The Province of Alberta

IN THE MATTER OF "THE NATURAL GAS UTILITIES ACT"

—and—

IN THE MATTER OF an Enquiry into Scheme to be adopted for Gathering, Processing and Transmission of Natural Gas in Turner Valley

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G. M. BLACKSTOCK, Esq., K.C., *Chairman*

Dr. E. H. BOOMER, F.C.I.C., *Commissioner*

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MR. STEER: Mr. Chairman, there is an admonition of Judges that we will hear the other side. It seems to me a very wise one because I have sat here for the last more than a week examining and listening to arguments based on the multitude of figures that have been submitted, I sympathize with the description that was given by Mr. Justice Jackson in one of the recent cases. The results are delerious that can be got from an examination of figures, whether they are drawn out of a hat or whether they are based on evidence.

It seems to me, sir, that there are a few broad general principles from which this question that you have to decide has to be determined and in putting those principles before you I should like first to say something of the history of this Turner Valley field.

I have no doubt that these facts are clearly in your mind but I think it might be advantageous if I did refer to them.

It is perfectly well known that the first gas that was supplied to the Canadian Western system came from the Bow Island field by means of the presently existing sixteen inch line which is the centre of the system.

Then there was a Board Hearing in 1921 as the result of which the Canadian Western Company was directed to augment its supply.

The Royalite at that time was producing gas from the three original Dingman wells and the result of that Board Order was the contract of December 1921, which is in as Exhibit 69. As a result of that contract Royalite built a

compressor station and the Canadian Western built a combination six and eight inch line connecting up with the Bow Island line at Okotoks and that contract contained an exclusive feature which is referred to in Section 67 of the Act which you are now dealing with.

The contract provided that the Royalite was to offer all other gas produced by it to the Canadian Western Company and that the price was to be 13 cents. That was the situation as it stood until October 1924 when Royalite #4 came into production from the lime and a new agreement was formed. Now it is said in this new agreement it is supplementary to the agreement of 1921.

I question whether there is any occasion at all to examine the 1921 agreement in the interpretation of this 1925 agreement and to suggest that it is the really controlling agreement at its date 1925. It again contained this exclusive feature and the price was 10 cents, reducing to 9 cents after certain production being taken and a ten inch line was built from Turner Valley to Calgary by the Canadian Western Company, and the Royalite Company built the Seaboard scrubber, reserving to itself the right to remove all gasoline and helium from the gas supplied to the Canadian Western system.

Well then in 1928, I am sure that is the date, in 1928 the fourteen inch line was built to Dewinton connecting up there with the main line from Bow Island and in 1928 we had the reduction in price to $7\frac{3}{4}$ cents.

In August 1930 the Bow Island repressuring contract was made between the Canadian Western and the Royalite Company and in that contract as the evidence shows gas was stored in the Bow Island field up until 1939.

It is fair to say that all through this

period and up to 1933 that probably the main interest of Royalite was the sale of gas to the Canadian Western system, although we do not know just what the amount of naphtha that was recovered by the way by the Royalite Company.

In 1933, however, in my submission the situation changed entirely. It was in that year that because of the increased richness of the gas and that appears from the evidence in several places. Perhaps I may mention pages 3325, 3326, Volume 43; 5523, Volume 68; because of the increased richness of the gas this absorption plant was built and from that time on the Royalite operation was as it has been very clearly described by Mr. Stevens-Guille an oil and naphtha operation with the good fortune of having a market for residue gas.

Now there is evidence that the capacity of this absorption plant was related to the peak demands of Calgary. Nobody disputes that. But I say that in the light of the fact that from 1933 to 1938 this Royalite Company over-produced the market demands of the Canadian Western system and all other systems by two billion feet and by reason of the fact that the Royalite Company in 1935 built #2 absorption plant and flared the gas from that plant, that it cannot be said that this absorption plant was an adjunct to any natural gas system. That evidence, in my submission, is conclusive to the fact that what the Royalite Company from 1933 on was doing was carrying on an oil and naphtha business with the good fortune of having a market for its residue gas.

You may wish to refer, Mr. Chairman, to Mr. Hamilton's statement WH 12, which shows that from 1933 to 1938 there was marketed by the Royalite Company 54,167,000,000 cubic feet and you will refer to Statement WH 11 which shows

that in the same period there was processed through the absorption plant 257 odd billion cubic feet. 54 billion as against 287 billion.

In those six years there was blown into the air more than half the amount of gas that is involved in this very long Hearing.

In addition, as I say, in 1935 there was the construction of this new plant which blew into the air still further very large supplies of gas.

Now it is true, it is true, that in 1938 the flare at the #1 absorption plant was discontinued. That at #2 plant was allowed to go on but the discontinuance of the flare at #2 plant and the acquiring of the gas cap acreage by Royalite that preceeded it was nothing more than, in my submission, an act of intelligent self interest on the part of the Royalite Company connected with its combined business of oil and gas.

And then we have in 1936 the discovery of oil in the limestone, crude oil in the limestone, and in 1936 we have the construction of the British American absorption plant blowing all its residue into the air. So that, having all these facts in mind, sir, I say we are absolutely justified in accepting as accurate Mr. Weymouth's description of this situation when he said in Exhibit 3 at Page 1:

> "The total production of natural gas has been dictated by the oil and naphtha operations rather than by the demands for gas as fuel".

Now as we know, Mr. Weymouth made his report and his report is implemented to some extent again as a matter of intelligent self interest on the part of the Royalite Company. There was the consolidation of the Royalite #1 and #2 plants.

There were the exchange of gas contracts between the Royalite and those other Companies. Mr. Weymouth also recommended the reduction of the B. A. and G. O. R. flares and he recommended repressuring, but he did not recommend as I might point out, he did not recommend the construction of that very troublesome low pressure system, which in my submission, is the cause of the greater part of the trouble we have had throughout this prolonged Hearing.

And I must mention the fact that prior to the enactment of the statute, Madison was incorporated as a subsidiary of Royalite and it acquired Royalite's gas division. That contract has had to be approved and the Board was very careful in the approving of it to reserve to itself the right to treat Madison and Royalite as an integrated undertaking, and the same thing happened as we have seen with regard to the B. A. Company and the B. A. gas Utilities Company, and in my submission in both those cases the situation that confronts us has got to be examined from the point of view of an integrated undertaking in each case.

Then came the statute and your Board was constituted and the purpose and intent of that statute is, and I think it is agreed by everybody, to eliminate waste.In the first place it is probably true to say as Mr. Davis said that the main purpose was conservation because we know perfectly well that for ten years before that the Government of this Province was trying to find some effective way to curb this waste, but there was another objective which everybody agrees was aimed at and that was the sharing of the market. I should like to point out that the market that was to be shared was the market for a product which up to that time had been blown into the air and wasted in a large measure.

It was a product which, notwithstanding the arguments which have been put forward here, had no cost. There was no market for it. It involved no cost. It was nothing but by-product and it is idle to suggest here as has been suggested particularly with reference to the south end of this field, that the price of gas at the well head has got to be fixed at such a price as will encourage other Companies to drill for it. Whoever heard of a well being drilled in this Province for gas ? We know perfectly well that it is not so. We know perfectly well that every well that has been drilled in this Province has been drilled for oil or naphtha and will continue to be so drilled.

MR. HARVIE: What about the Viking field ?

MR. STEER: We are not discussing that at the moment.

MR. HARVIE: You mentioned this Province.

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MR. STEER: I beg your pardon, Mr.Chairman, and I am quite sure you understood what I was referring to.

THE CHAIRMAN: Yes,but I was thinking of Medicine Hat.

MR. STEER: Well, I am talking about Turner Valley, and I am very sorry that I made the error and I will probably make more. And I say that gas is a by-product pure and simple of an oil operation in Turner Valley, and that is what all four of the people or groups of people who are interested there, all four of them, Royalite, British American, Gas & Oil Refineries and the well owners themselves have capital committed, and had their capital committed to these various undertakings prior to the enactment of this legislation.

Then I would like to point out to the Board what occurred at the Preliminary Hearing of May 1944, and I would like to remind the Board of the insistence of the British American Company at that time on the construction of this low pressure system which had not been advocated by Mr. Weymouth, and for that reason it was subject to all the closer scrutiny.

It is to be observed that in its Exhibit 1, its proposal, the B.A. Company sets out that the investment is not justified unless the low pressure scheme is adopted, and unless it is assured that so long as they will return the costs, the wells are going to be operated. And there are a number of passages in the evidence that was taken at that time to which I would like to refer the Board.

On page 12 of the record, Counsel for the Company said this:-

" It contemplates a very effective scheme for conservation of the gas within an area, or just a portion of the field, and as far as the economics is concerned it suggests that it can do it well within the price that is presently being paid by the Gas Company at the scrubbing plant so it should not disturb any situation from that standpoint, and the matter of price, we suggest that if there should be an increase in price that goes to the producer, not to us. Our scheme does not contemplate any change in price will change our set-up at all. I do not know that either the City or the Gas Company are materially affected by our scheme or an order allowing us to go ahead providing the Board is satisfied that it is a true conservation scheme. I think that is all that the City or Gas Company might be interested in so far as our scheme is concerned. The producers are interested and I understand they are represented here and some wish us to go ahead and deal with the matter and a lot of them would like to have our scheme presented so they can make up their minds as to whether they favour it or not."

At page 145 the Company asks for an Interim Order. At 145 and 146 the proposal is said to fit in no matter what the Order might be. At page 151 the construction is described as an emergency. At page 153 the British American scheme, Counsel states, can be implemented within the 7¾ cent price. At page 154 it is stated that the Company is satisfied that the Board will set a fair price for scrubbing, and that it is prepared to proceed on the

basis of receiving 7¾ cents at the scrubber outlet. At page 155 the Company submits an alternative proposal to instal the low pressure system. At 156 the importance of the low pressure system to the absorption plant is referred to. And the statement is made that the Company is prepared to take its chances. And at page 254 Mr. McCutchin is quite precise in stating that the Company is quite prepared to take its chances on the 7¾ cents price and on that basis could settle with the producers, indeed that he had done so.

Now, I am not sure, Sir, that I have got all the references there, but there are sufficient there in my submission to indicate that if it had not been for those assurances, and if it had not been for those undertakings, this low pressure system would never have been constructed, and if it had never been constructed all the problems would be very much simpler than they are.

The construction was completed and now the Board acting, as I see it, under Section 50, which gives it the power to fix prices and, as directed by Section 72, is confronted with the task of fixing a just and reasonable price for the services and commodities that are involved in this Hearing.

Now, I need not read to you, Sir, Sections 49(2), dealing with the rate base, and 72(1)(a) dealing with prices at the well head and at the outlet of the absorption plant. Those sections make it quite clear that this Board has an absolutely free hand in this matter provided that the rate base is based on a basis or formula. Section 49(2) makes it clear that you have got an absolutely free hand on the question of depreciation, including depreciation that has been taken with respect to these assets in

prior years by either the owner or the previous owner. As long as you have got a basis or formula with respect to your rate base, and as long as you have got a just and reasonable method or basis with respect to prices at the well head, and at the outlet of the absorption plant, because those are the only two prices to which 72(1)(a) applies, then, as I say, you have a free hand. And in exercising the powers that have been given to you, as the statute tells you, you are to have regard to all the circumstances and the factors involved.

Now, that section of the statute gives to the Board power, and a power which the Board ought to exercise, to consider in making its decisions the history of this field, the purpose and intent of the Act, the waste nature of the commodity that the Board is called upon to deal with, the possible effects on the Calgary system, the well head price in existence when the statute was passed.

The matters to be decided seem to centre around, first, the well head price or high pressure gas, divided into two classes, marketed and repressured; the well head price of low pressure gas, marketed and repressured; the price of conserved gas, and I am not going to say anything further about that, I am going to say simply that that appears to be a matter of contract between the producers and the purchasers, and it does not follow as a matter of course that that price for conserved gas is to be paid by the consumer. That is a matter, as I suggest, which should be decided after the terms of those contracts are settled.

Well then, in addition to that well head price we have got to consider a scrubbed gas price. The Board has power under 72 to determine the price for gas at the

outlet of the absorption plant, it is true, but I am suggesting that there does not appear to be any occasion for the fixing of that price. It seems to me that the price that we have got to concentrate on, the prices that we have got to concentrate on are, first, the well head price, and then the scrubbed gas price for gas delivered to the various markets.

Now, those markets are set out in Exhibit 55, Canadian Western, and in Canadian Western's market I should like to point out that in my submission the Canadian Western market includes the Imperial Oil Refinery, as I think everybody agrees, but I doubt if everybody does agree that it also includes the Alberta Nitrogen market. My submission is that there is absolutely no difference between the gas that is supplied to the Alberta Nitrogen Company and the gas that is supllied to the Imperial Oil Refinery, or any other large purchaser that is part of the Canadian Western market. And then there are other smaller markets to which I need not refer.

I propose then to deal with the well head price and the scrubbed gas price, but before doing so I think I should say something on the question of reserves.

Everybody seems to accept Dr. Katz' final opinion of 361 billion, but I think we should look at that figure with a degree of conservatism. It may be high, first, because the liquid loading may run up to 20% instead of the 10% upon which the figure is based. You may wish to refer to Exhibit 44, page 9, and pages 1079 and 1112 of the evidence. There is the possibility of the withdrawal of the Home gas. There is the possibility that much gas might be diverted to other uses. And for those reasons we suggest that perhaps the figure might be reduced to something below

361 billion. And even if the figure that is arr ved at should prove to be conservative, there might be advantages in taking accelerated depreciation in the earlier years of this project. So that my client submits, first of all, the wisdom of taking a smaller figure than 361 billion; secondly, in fairness to Madison, that that figure of 361 billion might be accepted as a basis for accruing depreciation up to this date; but, thirdly, the wisdom of taking some smaller figure for future throughput depreciation, but only provided that this can be done within the limits of the 7¾ cent price, because our submission is that that price is the upper limit beyond which the price ought not to go to this system. Our suggestion is that the Board might consider some figure such as 250 billion, provided it can be done within the 7¾ cent price.

And even if the price arrived at is below 7¾ cents, my client would not be indisposed to pay the 7¾ cents price subject to the approval of the City and of the Public Utilities Board, provided that any surplus over and above that price should go to a reduction of the rate base.

Now, we come to the well head price. My friends are unanimous up to date in saying that the price fixed for this waste product for the citizens of Calgary and the other consumers along this line, ought to be based on a price which is all the market could stand in that system, and then work back to get a price at the wellhead .

(Go to page 7148)

It is from that we get perhaps the most delirious results that have been put forward. I say that the proper starting point in the determining of these prices is the well-head price. I propose now to consider the well-head price of the high pressure and low pressure gas, and the scrubber outlet price and the price for repressured gas.

Madison and the British American Company take possession of this high pressure gas at the well-head and they process it subject to the payment of a price for its gasoline content, and subject to the payment of a price for a proper proportion of the high residue gas marketed and subject to a price for their proper proportion of the re-pressured gas. Very interesting legal questions arise as we attempt to follow the course of this gas from the well-head up to the point where it is delivered to the Calgary system. In my submission the simplest way to look at it is to say that Madison purchases this gas at the outlet of the separator at the well-head and it owns that gas up to the point where it is delivered into the absorption plant; that the absorption plant is the owner of the gas as it is passing through that plant and Madison becomes the owner of it again as it issues from the absorption plant. I submit that as they exist today the contracts as between Royalite, now Madison, and the well-owners are susceptible to that interpretation and there is no precedent cited and probably none presently exists for the fixing of a price at the well-head under the circumstances under which your Board is required to fix it. I would say one reason why no such precedent does exist is that what we are dealing with is essentially a waste product, for many years a by-product of the production

of oil and naphtha and clearly so in the case of British American and G.O.R. and the Producers. The only qualification to be placed upon that statement with respect to Madison and Royalite, viewing them together, in my submission is the fact that they carry on a combined business with a market for their residue.

Now what prompted the legislature when this Act was passed was a situation where Royalite had an exclusive market for residue gas. I submit that the evidence clearly discloses that for all practical purposes there was no other market. Any gas that did not get into that market which Royalite had, and there was a great deal of it, was waste, if we might properly apply that term with all deference to my friend, Mr. Fenerty, if we might describe gas as waste which has already performed the very important function of lifting oil to the surface and carrying naphtha to the absorption plant. It was that existing market of Royalite that the Statute was designed to share with other producers. The Legislature when enacting that Statute certainly, I submit, did not contemplate that the consumer on the Canadian Western system was to be compelled to bear all the traffic would bear for that waste gas, whether it is the 33 cent price mentioned by Mr. Zinder, which on his submission might just as well have been 53.6 cents, why it was not is a little difficult to understand except the delirious nature of the result. Whether it is that 33 cent price or whether it is the 5 cents that my friend, Mr. Chambers, picked out of a hat and says should be added to the consumers' price in Calgary. And I further say that the Legislature did not contemplate that this Statute was going to have the effect

of paying back to people who had their capital committed to undertaking a very large share of that capital at the expense of the Calgary consumer. What the legislature had in mind was conservation, sharing of the market which had been established and had been established with a price of two cents for residue gas at the well-head and it contemplated sharing in a fair way all costs by beneficiaries in proportion to the benefits received. That principle seems to be accepted by everybody connected with this Hearing, as it must be, although it is applied with varying results.

There are only two witnesses who attempt to deal with this question of well-head price seriously. One is Mr. Zinder and the other is Mr. R. E. Davis. They both deal incidentally and as a corollary to their discussion of well-head price with alternative uses and perhaps I might clear that question away first.

Mr. Zinder, in his Exhibit 126, and in his evidence, discusses three alternative uses, Carbon black, Fischer-Tropsch and Chemical industries. But if the Board will refer to page 1491 of the evidence, it is absolutely clear that he has made no study of this question at all and is incompetent to express an opinion.

Mr. Davis deals with the matter in Exhibit 148, page 12, but neither there nor in his evidence, nor in the evidence of any other witness is there any question of a present demand for this gas for use other than as fuel, if we except of course the war project, the Nitrogen Plant. The evidence as to alternative uses is of no value save, especially as the witnesses on behalf of the Ammonia Plant stated and as Mr. Davis stated, to indicate the importance

of low price if industry is to be attracted and if industry should be attracted to this very limited quantity of gas.

Coming now to the discussion by Mr. Zinder and Mr. Davis of well-head price, I am going to submit respectfully first that the Board may have some hesitation in regarding Mr. Zinder as an expert either on gas or coal. I am going to refer you to pages 4076 and the following pages and page 5010 and the following pages, where he is cross-examined as to his qualifications and I think it is fair to say that Mr. Zinder says himself that he is a paper man only, without any practical experience in either coal or gas. Whether he is an expert or not, in my submission, his evidence is of very little help, if any. He first analyses the cost of production of this gas and goes into the investment theory of prices for the purpose of rejecting it and nobody suggests that gas coming into existence in this way, in the way this gas in Turner Valley comes into existence, should be priced on any investment theory of prices.

In the second place, he deals with prices elsewhere. It is clear from his evidence that he neither knew, nor did he give to us the conditions surrounding the production of gas he speaks of, which he invites us to compare with the gas that is produced in Turner Valley. He admits that those prices are not helpful and that what the Board has to do is to arrive at a judgment figure. I am not sure that he is right in that in the light of what has happened heretofore with respect to this price.

In the third place, he discusses the price of competing fuels and elasticity of demand and he says that this fixes the upper limit of the price and he tells you that 53.6 cents in comparison with coal is the

price that you may fix in Calgary, although out of an abundance of caution he cuts 20% off that. Why, does not appear. Why 20 cents? It happens that it is said that the evidence indicates that there was a large consumption of gas at 33 cents, which is probably the reason why he adopts his 20 cents. It is clear, however, even from Mr. Zinder's evidence at pages 4079 to 4081 that under all the circumstances of this case, the law of supply and demand is a law which should receive very weighty consideration. My friend, Mr. McDonald, attaches a great deal of importance to this 33 cent price, which Mr. Zinder mentions. Really that price is, as has been pointed out, all the traffic will bear and it might have been much higher. One is tempted to ask someone for a sound reason why the citizens of Calgary and other consumers on the Canadian Western system, with an assured and comparatively long-lived supply of cheap gas at their doors, should now be asked to pay for a waste product all that the traffic will bear for the purpose of obtaining a small, remaining additional supply resulting to the people or other successors who are responsible for the waste of almost 5/6 of the total production of gas up to this date.

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What did Mr. Davis say ?

He said We are dealing with a conservation problem; that after conservation has been determined on, prices are to be fixed and costs are to be apportioned .

He said that competitive costs of coal and gas have no bearing;

That the coal dealer does not fix his price with regard to gas or electricity;

He says you cannot apply public utility principles for the reason that the wells were not drilled for the purpose of obtaining gas, none of them;

He says that the Turner Valley oil field gas is very comparable to oil field gasses elsewhere;

He says that in Texas nearly a billion feet go into the air from oil wells that the operators have wasted in the production of oil but they have learned to repressure and they prefer the benefits of the effect of re-pressuring that gas to sales in the market;

And he points out cases where wells, under conditions which I submit to be comparable to conditions here, justly comparable, of gas wells, of gas currently at $3\frac{1}{2}$ cents, which has to be compared with our $7\frac{3}{4}$ cents and in another case 3.4 cents, as compared with our $7\frac{3}{4}$ cents.

He says that he knows no way of making pencil figures to get the price of gas, that is waste gas. That the figure must be a judgment figure and that in getting that figure consideration should be given to the past resulting in lower pressures and increased costs of three hundred pound gas;

That the gas has to be gathered from many

wells and is sour gas and that he will consider the 7¾ cents, which has been in existence since 1928 and the 2 cent price which has existed since 1939 at the well head.

Now I want to say something about that 2 cent well head price;

We do not know the nature of the bargain which preceeded the fixing of it but we do know that it was fixed as a part of a voluntary conservation scheme by the largest producer of gas in the field; that that largest producer of gas in the field had full knowledge of the cost of processing and handling that gas and we have no doubt, we should have no doubt, that access to those costs show that the price as it was then agreed on by this largest producer was a fair price.

My learned friend, Mr. McDonald, acting for the other producers, has been astute to give the Royalite Company a reputation for fair dealing, which in my respectful submission it has earned over many years past, and I am going to ask this Board to say that that 2 cent price, under all the circumstances, fixed as it was, is a fair price in 1939 and is a fair price today for a waste product.

There is a burden, there is a burden in my submission, upon the producers in this case to show that that price is not fair and in my respectful submission there is not one bit of evidence in this long Hearing which will substantiate that allegation that it is not a fair price.

What the producers come in here and ask your Board for is to take that price which has been established by bargain and substitute for it an arbitrary figure picked out of a hat.

Bear in mind the conditions existing when this scheme was inaugurated, tremendous quantities of waste gas going into the air, the necessity for conservation, the necessity for expensive installations if the Producers and the absorption plants were to be allowed to continue their businesses as they had been in the past.

Now there were only two alternatives; We are either going to allow these people to go on and blow into the air these tremendous quantities of gas or we are going to conserve it and if we are going to conserve it we are going to do it in one of two ways:

We are either going to construct these installations or we are going to say to the people who are responsible for this waste: "Close down", and it might quite well be that in the interests not only of the gas consumers of this Province but also in the interests of the oil producers in this Province, it might have been well if the Government had said 10 years ago/that very thing, "Close down your operations or conserve this gas.".

Why, under these circumstances is the two cent price fixed in the way that I have described it, not a fair price for this gas?

I come then to the low pressure system:

Perhaps I should say low pressure gas, because what I have to say is applicable, as I think, and as I submit, not only to the British American low pressure system in the South End of the field but it is applicable also to the Gas & Oil Refineries' gas and it is also applicable to the No. 3 compressor's gas.

To rescue this gas, costly installations

have been made for the purpose of getting the gas both to the absorption plant and to the market and to the extent that it was necessary to make those installations for the purpose of getting the gas to the absorption plant and to the market the value of that gas is less than the value of the high pressure gas at the well-head.

I pointed out that conservation of this gas might have led to a direction to the producer to close down his plant. Instead of doing that, the Government said: "Go ahead.", at least the Legislature said "Go ahead and construct these installations and then establish the fair price."

The fair price for this low pressure gas, in my submission, Mr. Chairman, is the 2 cent well-head price established for high pressure gas less the additional cost of handling the low pressure gas.

Now my friend, Mr. Saucier, yesterday said or gave a figure of .88 and we figured out the other day that that might amount to as much as a cent in the case of the British American system but whatever the figure may be that is worked out by the Board as sufficient, my submission is this, that this low pressure gas should be the 2 cent well-head price established for high pressure gas less the additional cost of handling this low pressure gas.

As to the scrubber outlet price. The Board is dealing with a business which has both regulated and unregulated compartments. It is carried on in such a way that all agree that the costs ought to be shared.

This problem has been dealt with in the United States, in the United States Supreme Court, in very

recent cases and as is pointed out in the Colorado Interstate case, 58 Public Utility Reports at page 69, all that can be accomplished by an allocation of physical properties can be attained by allocating costs, including the returns.

It is clear, then, that there are two ways in which this problem of the allocation of costs can be dealt with: One is to segregate the properties and the other is without segregation, simply to make an allocation of the common costs.

And before dealing with whichof those methods ought to be applied, I would like to discuss with the Board the principles on which the common cost of these integrated undertakings should be divided, and what I have to say now refers particularly to the Madison plant, because I am going to submit that there are some special considerations to be applied to the British American Plant.

The Madison and the Royalite Companies, or rather the Madison and the British American companies, so far as their gas interests are concerned, are public utilities. So far as their natural gasoline businesses are concerned, they are not. The commodity which each requires, whether it is for its gas business or its natural gasoline business, comes from the same source and then the facilities which have been constructed by Order of this Board are useful to both.

The integration of the businesses and the connection that I refer to, is recognized by the companies themselves. Mr. Latham, for example, when putting Madison's proposal originally before the Board, Madison's proposal originally before the Board, proposed

that there should be a division of these common costs on the basis of sales realization of the products. He said that the division of the costs of the gathering lines and of the Numbers 1 and 3 Compressor Stations should be on the basis of sales realization. That was in May, 1944.

In September 1945, Madison and Royalite put forward an entirely different proposal. They say that Royalite is now a customer receiving a service, namely, the service of handling the volume of gas represented by plant vapours, natural gasoline absorption, boiler and electrical plant fuel and drilling fuel returned to the North end. Under this proposal they justify it by saying it is an application of the volumetric method of the allocation of costs.

In my submission there is only one thing which would justify the method that is proposed in that submission, - if the Madison Company carried for Royalite 15% of the gas that comes from the well and carried for Madison 85% of the gas that comes from the well, or whatever the percentages are. I propose to use 15% and 85% in the course of this argument, although I realize some of the figures would justify 17 or some other figure.

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If the Madison Company took 15% of the gas that comes from the well and delivered it into the Royalite plant and then took 85% of the gas that comes from the well and delivered it to the Madison system for use in the market there is a justification in that for the application of that volumetric method and that is the only way, in my submission, that the volumetric method could be applied to this situation because, what are the facts.

The absorption plant does not require simply the assumed 15% of that gas. The absorption plant requires every foot of the gas that comes from a well, every foot of it. And the gas that goes out of that absorption plant and is delivered to Madison is a very different thing from the gas that goes into it and incidentally is a gas with a much smaller b.t.u. content.

Royalite, in my submission, whether the agreements justify my conclusion or not, must be regarded as the purchaser of a commodity and that commodity that it purchases is 100% of the gas that issues from the well. It processes that commodity and it delivers the by-product of that processing to Madison to be furnished to the Calgary market. It requires 100% and not 15% and from every foot of that 100% it extracts components and the balance will be either used or flared.

And that in my respectful submission is a proper approach to this problem, whether we regard Royalite as the purchaser of a commodity or as one who purchases the service from Madison.

THE CHAIRMAN: And how would that argument apply to those lines which the Board ordered Madison to put in. We have

ordered them to put in lines.

MR. STEER: Exactly sir, and I submit the principle of the proper allocation of costs has been recognized by all parties whether a new or old construction and that you are fixing a just and reasonable rate base for Madison if you say to Royalite, you are going to pay for the benefit which you receive and that should apply, in my respectful submission, to both new and old construction.

The set-up today is exactly what it was in 1938 after the Royalite Company had adopted its voluntary conservation scheme, and for these reasons we submit that Royalite is more than fairly dealt with if the difference in composition of the gas entering and leaving the absorption plant be ignored and that Royalite's share of the common cost be fixed at 100 over 185 or whatever the proper fraction turns out to be on those costs.

Now it may be suggested and it has been suggested in the course of this Hearing that on this basis the absorption plant operation would not be a profitable operation.

With regard to that I submit that the absorption plant, the Madison operation, the Imperial Oil Refinery operation, are virtually one. They are acting together and have to decide profit or no profit, and we are not interested in that and I say in the second place that the proposal on its face appears fair and I say in the third place that if the service what is / is received the profit or loss resulting from the service is as has been pointed out on more than one occasion by Counsel for the Royalite Company a matter of no moment.

Then I say finally, a large part of these

operating costs are depreciation and return on Madison plant. These items are large because the Madison investment has been restated. It is perhaps that actually book depreciation shall be ignored and that depreciation be put upon an entirely different basis.

This depreciation and return which are allowed to Madison are received by it with one hand and turned over to Royalite with the other.

And then I should like to point this out that, whether the absorption plant operation is to be regarded as profitable or not will depend upon the price which it receives for its products.

Exhibit 177 was filed which indicates that if the Refineries in this Province had to purchase this absorption plant product which is necessary for their purposes elsewhere it would cost them just a little less than three times the amount which is credited to Royalite by the Refinery for the products which it sells.

So that if the real value of that absorption plant products were applied the figures as to whether or not the absorption plant could operate at a profit would be very different, so that I submit that bearing in mind the integrated nature of the undertaking, the favourable treatment that is proposed by this Company in respect to depreciation, the history of its operation, namely that the gas was wasted until enlightened self interest demanded conservation and that the logic of the situation in that the absorption plant is operated now just as it was in 1938 to 1944 and required all of the gas and not 15% of it. That, all these considerations suggest that at least 50% of the common costs ought to be borne by the

absorption plant.

Coming then to the question of the rate base on the assumption that 50% of the costs are to be borne by the absorption plant. There is an argument I would suggest for returning to the utility, that is Madison, only that part of its gas investment which has not been recovered from the $7\frac{3}{4}$ cent price.

In other words I say that there is an argument in favour of giving to Madison only the 41% of the amount of the original investment that has not been recovered through depreciation and that argument is based upon the fact that relations between Royalite and the Canadian Western since 1925 have been based upon the contract of that year and that that contract since that time has been under the control of the Public Utilities Board. That, at any time the Public Utilities Board could have intervened with respect to the $7\frac{3}{4}$ cent price and that the assumption to be made is that the $7\frac{3}{4}$ cent price was fair during all that time and that this 59% of its original investment that has been recovered through depreciation was really recovered from the Calgary rate and that consequently there was to be that justification for taking the books depreciation. But, whether that is so or not my suggestion then is that the Board ought to adopt as a value of the property that is included in the rate base, Mr. Hamilton's suggestion which is a combination of historical cost and reproduction cost new less depreciation, that $140,000.00 which is shown by him to be sufficient working capital and we have no objection to the addition thereto of the Girbotol royalty, but we do say that nothing should be included in that value for going value.

The Board will no doubt be looking at Mr. Hamilton's justification on Page 19 of his Exhibit 59, and his evidence as to the going value. My submission is that in rate cases the going value is the matter of cost and not of value at all. If you are going to say that because the business has been established and is earning money it therefore has a value greater than the value of its parts, then you are saying that it has the value because of its capacity to earn and you are including earnings as an element of value. And it is a well known fact that in no case - at least I submit this is so - that in no case are the earnings of a utility considered in fixing a rate base.

Barnes in the book that has been referred to deals with this question at Page 457, He points out that the proper approach to it is cost, not value. The same point is made in the Galveston case and a lot of these cases to which I refer, sir, are found in this collection of cases by Barnes on Public Utility Regulation which I shall be glad to leave with you.

In Barnes cases at Page 389, this is Mr. Justice Brandeis and it is from the Galveston Electric Company and the City of Galveston case and he says this:

> "The going concern value for which the master makes allowance is the cost of developing the operating railway system into a financially successful concern. The only evidence offered or relied upon to support his findings is a capitalization of the net balance of alleged past deficits in accordance with what was said to be the Wisconsin rule."

You will find, sir, the discussion of that Wisconsin rule in Barnes textbook at page 459.

"The experts calculated this sum in various ways. One estimate placed the development cost at $2,000,000.00; a more moderate estimate by the company's expert was $575,300.00; and the City's expert made a calculation by which he estimated this so-called cost at $212,452.00.

If the rule were that a prescribed rate is to be held confiscatory in case net earnings are not sufficient to yield 8% on the amount prudently invested in the business, there might be propriety in counting as part of the investment such amounts, if any, as was necessarily expended at the start in overcoming initial difficulties incident to operation and in securing patronage. But no evidence of any such expenditure was introduced; and the claim of the Company does not proceed upon that basis. What was presented by the witnesses are studies, on various theories, on what past deficiencies on net income would aggregate, if 4% were allowed as the depreciation annuity and 8% compound interest were charged annually on the value of the property used".

(Go to Page 7165)

Then the matter is dealt with from the same point of view and the West Ohio Gas Company case in Barnes Cases at 626; the Columbus Gas and Fuel Company case in Barnes Cases at pages 653 and 654; and the Natural Gas Pipeline Company of America case, in Volume 42, Public Utilities Reports, 139 to 141, and I will read a sentence or two from that case.

MR. CHAMBERS: What is the name of that?

MR. STEER: The Natural Gas Pipeline Company of America case and the Federal Power Commission, 42 Public Utilities Reports, 139 to 141. And there the passage reads at page 141. This is the Supreme Court of the United States.

A And this passage reads:

" Whether there is going concern value in any case depends upon the financial history of the business. This is peculiarly true of a business which derives its estimates of going concern value from a financial history preceding regulation. That history here discloses no basis for going concern value, both because the elements relied upon for that purpose could rightly be rejected as capital investment in the case of a regulated company, and because in the present case it does not appear that the items, which have never been treated as capital investment, have not been recouped during the unregulated period."

Those words could not have been uttered unless the rule is as I suggest it is, Mr. Chairman, that if you are going to get going value you are going to show that you spent the money. And there is no evidence in this case of the

expenditure of money for the purpose of getting those advantages which Mr. Hill refers to in his exhibit.

There is no objection to the balance of Mr. Hamilton's suggestion that reproduction costs new less depreciation should be applied to certain assets, but apart from that it is our submission that the only basis upon which the company is to be permitted to earn, and after all that is what your Board is defining, the value upon which this company is going to be permitted to earn, having regard to all the circumstances, including the circumstances of the integrated undertaking and the nature of the business, and that having regard to all those circumstances, historical cost is what you are going to apply in finding the amount on which the Company is to be permitted to earn.

Historical cost, whether of a business that comes under regulation for the first time, or of a regulated business, has been almost unanimously applied in this Province. Historical cost was applied in the original Canadian Western Hearing in 1921, as shown by the Exhibit 139. It would have been applied in 1926 in a case that involved the Western General Electric Company, and Red Deer, if the records of the Company had been sufficient to justify it. And as was then pointed out by the then Chairman of the Public Utilities Board, in one of the Canadian Western cases, the only cases in which historical cost is departed from, are cases where the records of the company are not such as to permit the Commission to arrive at that cost, and that is this case that I mentioned.

That is the case of the City of Red Deer and the Western General Electric Company, and that was in 1926, no, I beg your pardon, that was in 1924. The Board there says this:

" As to an investment made in a plant of this description it is usually given very serious consideration by Public Utility Commissions in arriving at the value to be placed upon a public utility plant, in applications involving the question of rates. This does not mean that the figures relating to actual investment, as disclosed by the books of a company, are taken as the controlling factor in arriving at the amount to be fixed as the fair value of the utility, but these figures, ordinarily, are given no little weight by Commissions arriving at a valuation of the plant involved. However, it may be said that, in this case, the company's books do not by any means afford satisfactory evidence of the actual bona fide investment of the company. Certain items charged up to capital investment, on their face, do not appear to represent any real asset,"

and so forth. And that indicates that what they would be looking for is historical cost if it could be found.

MR. CHAMBERS: What is that in?

MR. STEER: That is in a volume I have of the Alberta Public Utility Reports, 1923 to 1928, and the passage I read was at page 21.

THE CHAIRMAN: Who publishes that, Mr. Steer?

MR. STEER: I think H. R. Milner. He got that collection together, Sir.

THE CHAIRMAN: Even I do not have that in my library.

MR. STEER: Pardon, Sir?

THE CHAIRMAN: Even I do not have that in my library.

MR. STEER: I will be glad to leave it with you. Then in 1926, in a Canadian Western hearing, the then Chairman of the Board has this to say on this question, he said:

" The Board believes that in cases where the cost of reproduction has been found applicable,"

this is what I had in mind a moment ago,

" The Board believes that in cases where the cost of reproduction has been found applicable, it is largely because of either inadequate record of early investment, the implication of improvident investment in early stages, or of a very long preceding period during which much of the property representing original investment has disappeared from service in its original form."

Now, my learned friend, Mr. Chambers, as we expect from him, gave us a very masterful argument in which he defines the issues confronting us with clarity and conciseness and logic. I cannot say so much for his law, because the cases that he relied on largely, apart from United States cases, were those that involved expropriation and compulsory purchases, the wide principle of imminent domain. Now, everybody knows that the principle as applicable in those cases, is that the person who is deprived of his property is to be put in the position so that he is just as well off without the property and with the money as he would be with the property and without the money. Now, that is the principle named, as I see it, and I am suggesting to you that that principle has nothing whatever to do with the questions that are involved here in rate making.

My friend relies too upon what the Commission,headed by the late Mr. Justice McGillivray, did in the Pipeline Case, and they certainly did in that case reply on Smyth & Ames, and all the cases that followed it, and fixed reproduction cost new less depreciation as the basis. It might be that they were right in that case. I do not know. None of us know, unless we have gone through all the evidence in that case, but whether right or not, I say that the cases they relied on taken together make up what is known as the exploded present fair value concept in the way of fair rate making. And I say it is exploded in the way that the matter has been dealt with in the Supreme Court of the United States, from which theoriginal Smyth & Ames case came.

And with regard to that, and without reading it, I would like to refer the Board to a discussion of the present fair value concept that is found in Barnes Book on Public Utility Regulation at pages 370 to 403. And he states his conclusion in a very brief form. This book was written, by the way,in 1942. He states his conclusion in very brief form at 398, and I am submitting to the Board that the result of the recent examination of Smyth & Ames is this, that you can put out of that rule all the considerations that they were talking about with the exception of just two, the first is historical cost or prudent investment, whichever you like to call it, and the other is reproduction cost. Everything else it out of the window, as I read the modern attitude to Smyth & Ames.

Now, what Barnes has to say is this, at page 398:

" Despite the uncertainties and ambiguities that have been displayed in the foregoing cases, there has been some degree of crystallization in the thought of the judiciary. Certain of the original ingredients of the recipe have been consistently omitted: the market value of the company's outstanding securities is never used to measure the property of existing or proposed rates; the par value of outstanding securities is accepted as having probative force only when such evidence is acceptable to a commission, presumably because the securities have been subject to regulation; and the probable earning capacity of the property under existing rates has been deleted from the rule. Courts and Commissions have tended to place their reliance chiefly on two 'measures of value': the original cost, actual or estimated, to the present time; and the present cost of replacing the property; but the Supreme Court has quite uniformly held that fair value is not necessarily identical with either the original cost to date, the present cost of reproduction new, or the present cost of reproduction less depreciation."

And again at page 400 he says this, and in citing these texts, there are two texts that I have here, and I have not seen Barnes referred to in decisions of the Supreme Court of the United States, but Bonbright, another book to which I will refer shortly, has been referred to and relied on, and I am quite sure that you will find, if

you have not already seen it, that it is an extremely able and comprehensive discussion of all the matters that are involved in rate base making. Barnes says this:

" A critical analysis of the rule itself"

that is the Smyth & Ames rule -

"affords convincing evidence that the Court was not intent on prescribing a procedure for the future control of utility rates by State authorities. Of the six factors which the opinion enumerated as 'matters for consideration', not all of equal significance in furnishing evidence as to the fair value of a utility's property, and others afford no evidence whatever as to value. Two factors, the original 'cost of construction' plus 'the amount expended in permanent improvements' and 'the present as compared with the original cost of construction', in later application expanded to 'reproduction cost new' and 'reproduction cost less depreciation', have been widely employed as measures of present fair value. The other 'matters for consideration' are all unsuitable as measures of fair value for rate regulation; they seem to have been included in the enumeration only, because they appeared in the argument of counsel,"

and so on.

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He well and ably points out as Bonbright did in 1935 that what Commissions are interested in is fixing a value for rate purposes and not finding a value for any other purpose. All they are to do, and it is clear in my submission from this statement, and what the Board here has to do, what you are to do is to fix and determine, having in mind the complicated circumstances of this case, you are to fix and determine the value on which the utility should be permitted to earn a return. To fix and determine a value on which the utility be permitted to earn a return.

May I refer to what this writer, Bonbright - I said 1935 and it is 1937 - and since that time this book has been quoted on numerous occasions in the decisions of the Supreme Court of the United States. Here is what he has to say at page 1136:

> "The Lindheimer case illustrates the close interconnection between the treatment of depreciation as an item in the rate base and its treatment as an actual deduction from gross earnings. This relationship makes the former problem quite different from that faced by a commercial appraiser who is interested solely in determining the present value of old property without reference to any question of a fair return on invested capital. It shows the force of the economists' repeated assertions, so seldom frankly recognized by the Courts, that a valuation for rate making is an attempt to determine what the value should be rather than what this value "really is."."

On what amount should the utility be

permitted to make a return. And the same idea is expressed at 1154 and again at 1179. I will read from page 1179:

> "In most fields of law an appraisal represents an attempt by a tribunal to determine what value people do in fact attach to the property, or what value they would attach to it if they were to act as intelligent business men. In short, it is an effort merely to estimate value rather than to create or limit it. But in certain legal situations the valuation is meaningless unless it is thought of as a deliberate attempt by the tribunal to fix values rather than to find them."

Without reading them, I say that the same idea is found in these cases which you will find, Mr. Chairman, in the place that I cited. In the Minnesota Rate Cases, in Barnes at 384, Barnes' Cases, the Minnesota Rate Cases and the Georgia Railway Case in Barnes, at 396 and the Southwestern Bell Telephone Case in Barnes, 601, 602 and 605. I have no doubt that you will read, Mr. Chairman, the dissenting judgment of Mr. Justice Brandeis in the Southwestern Bell Telephone case, and probably have already done so. What I say is that that judgment contains perhaps the earliest expression of the principles upon which the Supreme Court of the United States at least has said that regulatory bodies ought to act. It is too long for me to read it and I am going to leave it and suggest to you that what the Supreme Court of the United States has done in the Hope case and in the following caseshas been to recognize the authority of that dissenting opinion. The Hope case is reported . . . . well, before we deal with the Hope case, I should have

mentioned its predecessor, which is the Natural Gas Pipeline Company case of America and that is in 42 Public Utility Reports. There are two or three passages which, with your permission, I will read. I am reading at page 136 of 42 Public Utility Reports:

"The establishment of a rate for a regulated industry often involves two steps of different character, one of which may appropriately precede the other. The first is the adjustment of the general revenue level to the demands of a fair return. The second is the adjustment of a rate schedule conforming to that level so as to eliminate discriminations and unfairness from its details. Such an orderly procedure for establishing the rates prescribed by the act would seem to be an appropriate means of carrying out its provisions."

I think I detect an error in grammar that is used there.

Then page 138:

"The Constitution does not bind rate-making bodies to the service of any single formula or combination of formulas. Agencies to whom this legislative power has been delegated are free, within the ambit of their statutory authority, to make the pragmatic adjustments which may be called for by particular circumstances."

Your authority is very wide.

"Once a fair hearing has been given, proper findings made and other statutory requirements satisfied, the courts cannot intervene in the absence of a clear showing that the limits of due process have

"been overstepped. If the Commission's order, as applied to the facts before it and viewed in its entirety, produces no arbitrary result, our inquiry is at an end."

And then at page 147. I have no doubt you, Mr. Chairman, will read this judgment and I will not weary you by reading much more of it, but I do want to read this at page 147:

"We have here, to be sure, a statute which expressly provides for judicial review. Congress has provided in Section 5 of the Natural Gas Act, 15 USCA 717d, that the rates fixed by the Commission shall be 'just and reasonable.' The provision for judicial review states that the 'finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive.' But we are not satisfied that the opinion of the court properly delimits the scope of that review under this act. Furthermore, since this case starts a new chapter in the regulation of utility rates, we think it important to indicate more explicitly than has been done the freedom which the Commission has both under the Constitution and under this new statute. While the opinion of the court erases much which has been written in rate cases during the last half century, we think this is an appropriate occasion to lay the ghost of Smyth v. Ames, which has haunted utility regulation since 1898. That is especially desirable lest the reference by the majority to 'constitutional requirements' and to 'the limits of due process' be deemed to perpetuate the fallacious

" 'fair value' theory of rate making in the limited judicial review provided by the Act."

Now I think you will find, Mr. Chairman, that in most of these cases, I think in that case and in the Hope case undoubtedly and in the Colorado Interstate case, which I am going to refer to, and the Panhandle Eastern Case - those were all cases of regulation for the first time. I will simply refer you to Hope, 51 Public Utilities Reports, 193 and especially at 199, 200 and 201.

I would like to refer also to the Colorado Interstate case at 58 Public Utilities Reports, 65 and the Panhandle Eastern, 58 Public Utilities Reports, 100, all of which in my submission support this proposition that your Board is not bound by any formula and that you are free to consider all the circumstances including the inter-relations of the various proprietors and your having in mind all those complicated circumstances to fix the amount of money on which, in your view, these utilities ought to be permitted to earn a return.

Then having that principle in mind, I ask where any injustice, where any injustice would be done if Mr. Hamilton's suggestion as to the value of property should be accepted, and with respect to that I would ask you to look at Statement WH-9 which Mr. Hamilton gives in Exhibit 144 as to index prices. I have pointed out that the objections to Reproduction Costs New as to depreciation have been most fully and ably stated by Mr. Justice Brandeis in the South-Western Bell Telephone case, but he omits to state one which your predecessor, as Chairman of the Public Utilities Board, did refer to in the 1921 Rate Hearing of the Canadian

Western Company and that is this. Perhaps I had better give you the reference. It is at page 13 of that judgment. He says:

"Mr. Weymouth stated that this same principle should be applied in arriving at the value of a utility during periods of low prices as during a period of high prices. Anyone who supports this theory must of course make this submission in order to be logical, yet to carry out the theory in such a case would result in the wiping out of any utilities that may have been constructed during the period of high prices. As was said by the California Commission in Southern Sierras Power Company (referred to in Public Utilities Reports, 1921, p. 218), 'If present values be regarded as the proper rate base during periods of high prices, it should likewise be so regarded during periods of low prices and rates reduced accordingly; under present conditions applicants might repay temporary advantage were this suggestion followed. Applicants in the past have depended, and in the future will probably depend, largely upon borrowed moneys for their development. The present development made at large cost might readily under the 'present value' basis, shrink in 'value' to an amount below that of the bonds outstanding, and cause either a period of temporary inability to develop or an actual failure, with the accompanying difficulties and losses."

(Go to page 7178)

In other words, if you are going to take reproduction costs new it has to be applied uniformly throughout the field and if you are going to base the rates on reproduction cost new in a period of high prices you have to base the rates of reproduction cost new in periods of low prices, but you simply cannot do it in periods of low prices because you have the paramount duty of keeping the utility in business and you cannot possibly treat the public and the utility fairly by applying that reproduction costs new theory throughout the whole history of the undertaking and in my submission, Mr. Chairman, that is the most powerful argument there is for using historical costs and I say that Mr. Hamilton's evidence indicates that there is no unfairness whatever coming to this Company in adopting his rates and so I say we should have these adjusted historical costs as the rate base.

"Prudent Investment"

How are you going to fix the rate base on the prudent investment principle ?

I have pointed out that you might segregate the assets used and useful or alternatively allocate the costs.

Assuming an even division of the common costs of Madison and Royalite, in our submission it would be fair to allow Madison as the rate base 50% of the cost of the old and new gathering lines; 25% of the service unit, in each case of course less accrued depreciation.

I say this would be fair: 50% of the cost of old and new gathering lines, subject to depreciation, and excluding from that the residue gas unit and the #3 compressor.

25% of the service units. 100% of the scrubber. 50% of the #3 compressor unit treating wet gas.

100% of the #3 compressor unit treating dry gas.

Now that involves the splitting of the rate base.

The alternative is simply to say that the rate base shall be accepted on Mr. Hamilton's figures and the capital charges and operating costs, the common element, shall be divided in the proportions that I referred to.

So long as the Royalite plant remains in business, it does not appear to make a particle of difference which one of those schemes is adopted but having in mind the suggestion that the Royalite plant might not remain in business it would seem to be fairer to the consumer to adopt the first one, that is splitting the rate base, than the second, because if you do that and the Royalite should, - if you do that and then the Royalite plant should go out of business, then they will take their own capital loss and it is the simpler way to do it too, because if you adopt the second one and then the Royalite plant goes out of business, then you are faced with the very difficult problem of then saying whether or not the Calgary consumer is going to assume all this capital loss or not because undoubtedly Madison will come before you and will say that "Now Royalite is out, all these costs certainly ought to be borne by the consumer" and you would have the difficult task of saying "No, you will not get any different treatment today than you had when your parent Royalite was in business."

Then on the question of "Depreciation".

Should historical costs be depreciated ? My friend, Mr. Chambers says "No" and he bases his argument on what was done in the original Canadian Western case, but the reason why depreciation was not allowed or was not taken in

the 1921 Canadian Western decision is clear from the judgment itself and it was this, the reason was this: Mr. Weymouth had given evidence and he apparently at that time was an advocate of the immortal plant theory, and he said that because this plant had been maintained 100%, that therefore there was no occasion for taking depreciation and I had better refer particularly to what he said, at Page 12 you find that about the statement and then at Page 16, the Board says this:

> "The Board thinks further that in view of the evidence as to the condition of the plant and in view of the principle adopted in arriving at the valuation of the system, that it should not make any deduction for depreciation."

Now that is a pretty complicated question because the evidence was not very wsatisfactory as to that.

MR. CHAMBERS: He used "Prudent Investment".

MR. STEER: In view of the principle adopted in arriving at the valuation of the system, but what I am suggesting is that that is a complicated question. He used "Prudent Investment" it is true, but the reason why he did it is a long story.

Now in the Colorado Interstate case, 58 Public Utility Reports at Page 80, you have a case here of regulation for the first time, actual legitimate costs as the basis of the rate base and actual legitimate costs depreciated,

At Page 80, the Commission found the actual legitimate cost of Canadian's property, including its producing property and gathering facilities, to be $10,784,464.00 as of December 31, 1939. It deducted over two million for accrued depreciation and depletion.

And the same thing appears in the Panhandle Eastern case in the same volume at Page 109.

All I have to say about that is that modern thinking seems to have advanced a good deal beyond Weymouth's immortal plant theory.

Assume then historical costs as the basis.

Mr. Hamilton recommended depreciation on the throughput basis and he admits he depreciated his assets in the order that those assets were acquired and put into the system. One wonders whether this method gives sufficient weight to the book depreciation which was taken by Madison and Royalite combined, regarding the business of developing a wasting asset.

In looking at that question you have to consider the waste and use of gas from 1933 to 1938, to which I have referred, and the waste that appeared prior to 1933, and the resulting, the result of the waste being to the benefit of and profit of the absorption plant and well owners, and the result of this is an increase in the present burden on the consumer and the suggestion now is that those who were responsible for this are to recover through the rate base all but 18% of their capital investment, while the books show that they have recovered 59%.

My submission is that good practice would have required the Royalite, when it started in to develop this field, to estimate the amount of capital which would be required over the whole life of the field and then if they are applying throughput depreciation to apply it on the basis of that amount of capital.

That is what apparently was done in the Natural Gas Pipeline case and it seems to be logical. As I say,

it was what was done in the Natural Gas Pipeline Case and appears at Page 141 of the report in 42 Public Utility Reports:

> "The Commission took as the amortization base the sum of $78,284,009.00. This was made up of the Companys' total investment, at the end of 1938, of $67,173,761.00, without deduction of property retirements already made, plus estimated future capital additions through 1954, including replacements, amounting to $12,159,380.00, less estimated salvage at the predicted end of the project in 1954."

It may quite well be that the 59% depreciation which has already been taken by the Royalite was based on some such theory and practice and I point out that the Board has very wide powers under Section 49, sub-section 2, to consider all these circumstances and in doing so I am suggesting, respectfully, that a good deal more weight should be given this question of book depreciation than my friend Mr. Hamilton has done.

THE CHAIRMAN: Two o'clock.

(The Hearing was here adjourned to be resumed at 2 P.M.)

(Go to Page 7183)

2 P.M. SESSION
June 18th, 1946

I have suggested, Mr. Chairman, that more weight than Mr. Hamilton has done might well be given to the depreciation that has already been taken by Royalite in its books. I submit that greater weight might be given either by increasing the amount of depreciation which Mr. Hamilton has allowed or it might be a circumstance to be considered when making the split between the gas and the gasoline costs.

There is no objection on our part to the 9% overhead which Mr. Hamilton has suggested ought to be allowed, nor is there any objection to his proposed $140,000.00 working capital and I have already dealt with the question of going value and submitted there is no occasion in this case for allowing any amount for going value.

So far as the rate of return is concerned, my learned friend Mr. McDonald referred to the Bluefield case, which I agree with him is probably the best authority on the question and you will find it, Mr. Chairman in that collection of Barnes' Cases at Page 496.

The rule appears to be that rates ought to be consistent in businesses having corresponding risks and uncertainties. My learned friend Mr. Chambers claimed 9½% return. Whether that is the right figure or not is something of course that the Board must in its judgment decide, but I must protest against the endeavour made by my learned friend to support that figure of 9½% by his suggestion that my client has been making that amount or more on its rate base.

My learned friend filed Exhibit 180, and as I understand him he contends that the figures on that Exhibit

show that my client has made a return of 12.45 down to 7.67% on its rate base.

I perhaps need not argue to this Board the fact that the corporate balance sheet from which my learned friend gets his figures has little if any relation to a rate base or has little or any relation to any rate making structure. The rate base and the permitted rate of return are not in any way reflected in my submission in the balance sheet of the Company. The property values for balance sheet purposes may be arrived at on the basis of appraisal, historical cost, replacement cost or in any other way and whatever method may be adopted for balance sheet purposes does not bind the Board, and in fact the Board, as you know Mr. Chairman, will pay no attention to it.

THE CHAIRMAN: We prefer the report made by the Directors rather than the balance sheet.

MR. STEER: Yes sir. In the same way the profit available for surplus as it appears in the profit and loss statement has no relation to the permitted rate of return or earnings applicable to net rate base. To reconcile the two there has to be many additions to and deductions from the profit available for surplus. It is conceivable that the Company would show a book loss and yet show a handsome return on the rate base and vice versa.

I am instructed to say, sir, that the return on this Company's rate base has never exceeded 7.1% and has fallen as low as 5.3% during the last seven years.

MR. CHAMBERS: The net rate base ?

MR. STEER: I did not say of a net rate base. I say that you have no right to assume that the rate of return [illegible], was as you suggested.

My learned friend also put forward Exhibit 182 showing the supposed effect of the arbitrary 5 cent increase in price on this system. He found that by raising domestic and commercial rates 5 cents per MCF, by utilizing the alleged excess earnings of Canadian Western, which happened to be non-existent and by substantially raising the rate to the Ammonia Plant it is possible to pay for gas delivered into the Canadian Western system 12.347 cents.

In accordance with Exhibit 178, Canadian Western sales to customers other than Imperial Oil and Alberta Nitrogen in the year 1948 will be more than three million MCF, less than in the year 1945, three million MCF.

THE CHAIRMAN: Is that on the loss of the industrial load ?

MR. STEER: The loss I think is the commercial load but the figure in the Exhibit shows three million less consumption.

Assuming that this lost business would,having Mr. Chambers' rate of at least 30 cents, the decrease in consumption would result in a decreased revenue to my clients of $900,000.00 and the only offset to that would be the proposed 6 cent price that is to be paid at the wellhead on their supposition $180,000.00, making the net loss of $720,000.00, and that net loss of $720,000.00 in the year 1948 can be recouped to my clients only in the price and on the nine million consumption it would require an 8 cent increase in price so that instead of the 30 cents in 1948 we have got a 38 cent price.

And it is also pointed out I should add too that if in 1948 the average rate is still further increased then that 38 cent price goes up accordingly.

THE CHAIRMAN: Mr. Steer, I cannot help thinking, and I

have mentioned it before. I follow your argument. I see your point quite clearly but everything that I use, everything that we all use has gone up in price very substantially in the last three years and I have asked the question before and I ask it again, why must the price of gas remain static when everything else goes up ?

MR. STEER: If there are corresponding changes and under conditions which necessitate the increase in the price of gas well and good. My argument is that there has been nothing shown in this case which will justify such an increase in price and I am starting my argument from the proposition that there is nothing shown to justify an increased price at the wellhead and once we start from that proposition we are going on the basis of costs and the proper allocation of those costs and all I am saying now is that my learned friend Mr. Chambers figures do not justify and do not lead to the conclusions that he would ask this Board to draw from them.

He says the 30 cents can lead to a price of 12.347 cents. I say on the figures that are before this Board in 1948 it will require a 38 cent price to lead the business up and I say if the Ammonia Plant was off then we will still need a higher price than 38 cents. Now is there anything to justify it ? I say no.

THE CHAIRMAN: Except what the Statute tells me to do.

MR. STEER: Yes, and my argument is based on the proposition that if you do what I suggest you are, fixing a just and reasonable price on the only available evidence that there is before you, sir.

Now then, I would like to say a word on income and excess profits tax, not because I am particularly interested in this here, but I may be concerned in another

Hearing and I would dislike to see the Board make an improper application of the principle in this gas case which might create difficulty in another.

What I suggest, sir, is that modern authority is to the effect that income and excess profits taxes normally or abnormally are to be allowed as costs. It is true that in the Valley Pipeline Hearing the Board there said that all income taxes normal or abnormal should be allowed as an operating expense, but that due regard should be given to this factor in fixing the rate of return.

My proposition is that the latter part of that statement in principle should not be adhered to. My suggestion is that taxes are a cost and that a Utility is entitled to recover its costs and that any decision on the question of income and excess profits taxes ought to be dealt with in the way in which it was dealt with in the Galveston case. It is in this book of Barnes, at Page 391.

THE CHAIRMAN: Is it in the Public Utility report ?

MR. STEER: Yes, I am sure it is, but I think I have the citation there. It is in 258 U.S., S.C.R., but it is at Page 391 in this collection of cases of Barnes, and what ho says is this:

> "The company assigns as error that the master allowed, but the court disallowed, as a part of the operating expenses for the year ending June 30, 1920, the sum of $16,254, paid by the company during that year for Federal income taxes. The tax referred to is presumably that imposed by the Act of February 24, 1919..... which, for any year after 1918, is 10 per cent. of the net income. In calculating whether the 5-cent fare will yield a proper return, it is necessary to deduct from

gross revenue the expenses and charges; and all taxes which would be payable if a fair return were earned are appropriate deductions. There is no difference in this respect between state and Federal taxes, or between income taxes and others. But the fact that it is the Federal corporate income tax for which deduction is made must be taken into consideration in determining what rate of return shall be deemed fair. For under Sec. 216, the stockholder (400) does not include in the income on which the normal Federal tax is payable dividends received from the corporation. This tax exemption is therefore, in effect, part of the return on the investment."

The question is dealt with in a very interesting decision in the Michigan Supreme Court that you will find in 54 P.U. 65 and in that case the Court divided 4-3 and the majority said this:

> Excess profits taxes are voidable taxes and the Commission should have considered whether or not it would direct a reduction in rates so as to avoid the taxes and it referred the case back for the purpose of having that question considered."

The three man minority, in my submission, treat the matter in a much more logical way. They say that the Utility should receive its cost. That taxes are cost and can be nothing else.

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And they say that there is nothing in the Galveston case to support the proposition relied on by the majority, and that when the Galveston Case was talking about taxes. it was talking about normal taxes, and they say, this minority says, that all prices are within the authority of the Galveston decision.

As to repressured gas, that is the fourth point that I have to consider, our position with regard to this is stated, and very well stated, by Mr. R. E.Davis in Exhibit 148, page 12, and at page 5503 of the evidence. He says that Mr. Weymouth's principle that costs should be borne by the beneficiary is fair, everybody admits that, and he says that the cost of this repressured gas or, at least, a great part of the cost, has to be borne by those responsible for the waste, and the necessity of the scheme of conservation was so as to enable them to continue in business to produce oil and naphtha. And he says that unless the consumer, and I submit that this is common sense and reason, that unless the consumer can get a firm assurance that he is going to get this gas, then he should not be saddled wih any part of the cost, Dr. Katz to the contrary notwithstanding.

What we say is that the situation should be examined when the contracts for repressuring are finally settled and then the cost should be divided in accordance with the benefits. If the consumer is assured of an increased supply, let him bear the share, but do not overlook the benefits that go to the absorption plants and the producers by reason of this repressuring scheme.

The South End low pressure scheme and the repressuring scheme there, were adopted at the request of

oil operators and the B.A. Absorption Plant. The main object was to get a share of the market for that gas. The consumer had no part in originating that scheme, nor is there any assurance in the scheme, as it has developed to this date, that the consumer is going to benefit. Dr. Katz expressed the opinion that this cost ought to be borne by the consumer. Surely, I mean, surely I mean if the consumer were going to get the benefit, surely he did not mean that the gas was going to be repressured and at some time in the future was going to be supplied to the Fischer-Tropsch Plant, and in the meantime the consumer in this Calgary system was going to pay for it.

We have no quarrel with the proposition that if the benefit to the consumer can be shown, he ought to pay, but we say too, if he is shown to be a beneficiary he should pay only in the proportion which his benefit bears to the benefits which the other beneficiaries receive. From a practical point of view, I suppose that the benefit of the well owner from this scheme might readily be deducted from the well head price of his gas once it has been determined.

Dealing now with those special considerations which apply to the British American Absorption Plant. I say this, in the first place, that on the principles that have been discussed of use and useful property and benefits, there would seem to be no reason, no logic, in the proposition that the consumer of the Canadian Western system should rescue the British American Company from expenditures which it made in gathering lines and compressors in 1936. Obviously, from 1936 until this scheme came into being, the capital of the British American Company was committed to that undertaking as a natural gasoline undertaking. And I ask someone to show me some good reason why now the consumer is going to

repay to the British American Company the money which it had irrevocably committed to that scheme prior to the coming into force of this Act. The British American Company, it would seem, is sufficiently compensated if at the expense of the consumer as is proposed a market is found for that residue gas which up to that time it had blown into the air. I say that the gathering lines of that British American Absorption Plant, the old high pressure gathering lines, should be excluded entirely from the rate base.

Then I suggested already that equity demands that the Company be held to its estimates, with regard to the construction costs and the other costs, with regard to the low pressure system, and I say nothing more with regard to that.

I have discussed the question of the principles which ought to be applied, in our submission, to the allocation of costs, and now approach the question as to what special considerations in that regard are applicable to the British American Company. And the first one appears to me to be this, that the low pressure system, on the Company's own evidence, increased the life of the absorption plant three times, from a life of three to three and a half years it has attained through the low pressure system a life of ten years. There seems to be no dispute about that, and I say this, Mr. Chairman, that if 50-50 is a proper division of the common costs between Madison and the Royalite plant, as we submit it is, then some larger proportion than the 50% of those common costs ought to be borne by the B.A. absorption plant. And I suggest that that is a matter which you will have to consider in the basis of the figures and perhaps arrive at a judgment figure, which, in my submission, might easily impose 75% of

those costs, or 60% of those costs, on the absorption plant in lieu of the 50% which we propose should be borne by the Madison.

So far as the transmission lines of the B.A. absorption plant to the Madison scrubber is concerned, that is an erection that was made for the purpose of rescuing gas, and we must, I think in fairness, regard that as a proper charge against the gas business.

THE CHAIRMAN: And what about the compressors?

MR. STEER: And the compressors in that line that are used for that purpose, but the compressors in that line that are used for repressuring should be dealt with on the same basis as the repressuring costs are dealt with.

Now, on the application of these principles, modified as now suggested, because of the special considerations applicable to the British American Company, the Board might either construct a split rate base or allocate costs on the corresponding basis.

The British American puts forward Exhibit 184 as an application of the demand and volumetric principle to this allocation of costs. And I suggest to you, Sir, that there is absolutely no ground for the application of that method of allocation to these costs. The only suggestion that has been made is that because Mr.Zinder put forward that method as a means of allocating costs of re-pressuring, that therefore it ought to be applied both to repressuring and to this British American situation. Now, my respectful submission is that it cannot have any application to either. Both the repressuring scheme and the British American low pressure scheme were dictated as to costs and capacityand everything else, not by the demands of the Calgary

market; they were dictated by the amount of gas that was produced along with oil and naphtha in the area served by them, and if you are going to apply the demand and volumetric rule, let the people who were responsible for this volume, namely, the oil operators and the absorption plants, absorb it. What right in reason or in logic is there to say that the Calgary consumer, who had nothing in the world to do with the development of that, is to bear the cost either of repressuring or of this low pressure system. The rule is not scientifically applicable, in my respectful submission, to either one or the other, and I submit that I have suggested to the Board the rule that properly ought to be applied.

Similarly, in the case of the high pressure compressor station, there is no room for the application of the principle there. That high pressure compressor station was geared to the outlet of the B.A.Absorption Plant, and the amount of gas issuing from the B.A. Absorption Plant was geared to the production of oil and natural gasoline in the area which was served by it. What has the Calgary market got to do with it?

I say then Sir, that the Board, in considering this matter, ought to give careful consideration to the more conservative value of reserves than the 361 billion. I say that the well head price of high pressure gas ought to be fixed at not more than 2 cents on the basis of the evidence that is before you. I say that reason and logic demand that that 2 cent price in the case of low pressure gas be reduced by the additional cost of handling it over and above the cost of handling high pressure gas.I say that

on reason and authority the rate base ought to be fixed on historical cost with such adjustments as Mr. Hamilton has suggested; and I say that you are free, either to split that rate base in proper proportions, or split the costs of handling the operation in those same proportions, and that the interests of the consumer would be more adequately served if the split rate base idea were adopted.

I say that we have nothing to do up to date with the repressured gas costs, and could only have to do with a portion of those costs provided we were assured of the ultimate receipt of the gas.

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THE CHAIRMAN: Thank you very much, Mr. Steer. Mr. Fenerty?

ARGUMENT BY MR. FENERTY.

If it please you, Mr. Chairman, I propose to deal with this subject in a somewhat different approach from most of the others. I feel that the various figures have been exhaustively analyzed and, like Mr. Steer, I propose to discuss principles which my associates and myself feel should determine the computations and allocations that should be made and not the details of those allocations. Where I have a different approach to any proposition from that of Mr. Steer, I will say so. We are in general agreement as to the chief principles governing this matter and where I do not refer to the points made by my friend Mr. Steer, I can be taken to be in accord with him and that I do not refer to them merely because I feel repetition by me and perhaps in not as well chosen language, would add nothing to what he has said.

In the first place, I think it would be not out of way to say something about the position of the City of Calgary in this Inquiry. We say, and I think after hearing arguments of my various friends here that we are in practical accord, in that the Turner Valley gas is not dedicated to this City, though that suggestion is now being made in the declining years of the field. We say that it necessarily follows from that that neither this City, nor the gas consumers in this City, are dedicated to the support of the well-owners in the Turner Valley field, or to the purchase of gas from the Turner Valley field. Those are obligations which can only be mutual. We agree that at one

time such a situation did exist by virtue of a contract involving the gas supply from Turner Valley at a price. There was a time when gas in the Turner Valley field was dedicated to the City - and when I say the City of Calgary I am referring to all of those on the line, but it is more convenient instead of referring to Lethbridge and so on each time I speak to just refer to the City of Calgary. There was a time when part of that supply was so dedicated but both the protection afforded by and the obligations imposed under those contracts have been done away with by the Legislature. It follows that no one is now bound to supply gas to this City except by direction of the Board, nor is the City nor the Gas Company bound to take gas from the Turner Valley field, and both must necessarily be entitled to look elsewhere. That poses a problem, I submit, to this Board far beyond the mere problem of saying what does this all add up to. If it is 33 cents it is going to be 33 cents. If it is a dollar it is going to be a dollar. It poses a problem that I propose to deal with a little later as to how much money will be available and what are the consequences of a rate which forces the City and the Gas Company to look elsewhere and in this day of almost daily discoveries of new supplies of gas. What are the problems of keeping the dry gas industry of Turner Valley on the rails so that some rate may be found which will not drive away the consumer and will still enable repayment to be made of at least those portions of the expenditures which have had the sanction of the Board. Now I said a moment ago that by virtue of contract which amounted to a dedication of a portion of the gas to the City we had gas at a price, which was a contractual price. That is what

the City is interested in today, what it had before the abrogation of these contracts and that is gas at a price. It is still interested in gas at a price. It is also interested in common with other residents and citizens of Alberta in the conservation of a natural resource. That is conservation of a resource in the sense that it shall not he wasted. In that it apparently shares the same views as the Government and that may be a Provincial Government matter. As individuals or as a City, and as representing the individuals in it, we are interested in gas at a reasonable and fair price; certainly not in gas at a price beyond that which could have been obtained as a matter of contract and certainly not in gas at a price which is increased by reason of any protection that is going to be given either the gasoline industry or the oil industry.

Now I do suggest, sir, that so far as the matter of Government policy is concerned in the conservation of a natural resource of this Province, that is a natural resource which it may be government policy at a later date shall be used in any place other than the furnaces of the City of Calgary. I do not know and nobody knows. That is something that may be remote in the future but it is not impossible.

You will remember that Mr. McDonald pointed out at one stage his interpretation of the purposes of the Government and there were two or three things he mentioned in particular, allowing the producers generally to share the market and providing access to it. Now if those are not matters of obligation of the producers, they certainly are not matters of obligation to the consumers,

to allow the producers to share the market. If on the other hand they are matters of Government policy that is a matter of Provincial interest as a whole.

This Inquiry was not instigated by the City of Calgary or the present users of gas as a fuel. I suggest that the City of Calgary has never said "This gas must not be flared." Gas is being flared today, 20 million cubic feet. A little while ago it was 25 million cubic feet. The City is not coming to the Board and saying: "This must not be flared."

We recognize it is being flared as an incidence of the primary purpose of this field, that is the production of oil. We have never said that the gas is allocated to us and we are going to have it, no matter what it costs. On the contrary the City has maintained that the opposite stand. From the time that its protection by way of contract as to the cost of gas to the Canadian Western Company was removed, it has taken exactly the opposite position to that, that it was entitled to have this and it would have it, come what may, and no matter what the cost might be. Such is the position as outlined by Mr. Stanley Davies in the early part of this Inquiry, before I had the privilege of participating in it. Amongst other things, he pointed out we are not interested in extremely high priced gas at this time. That was at pages 199 and 201 in Volume 4. My reading of the evidence indicated he opposed both the B.A. and the G.O.P. Plan. His opposition was registered at page 287, Volume 5. He suggested that both of those plans were against the interests of the consumer at pages 202 and 203 of Volume 4. Ralph Davis took the same position

at page 350 in Volume 5.

Now on the other hand, while these individuals, the individuals of the City of Calgary were opposed to these proposals so far as the consumers were concerned, the advantages of the proposals were recognized from the beginning by the oil and gasoline industry. While they were opposed by the City they were earnestly advocated by the producers and I refer to Mr. McDonald's remarks at pages 470 and 471 in Volume 6. Mr. McDonald, with commendable frankness, yesterday very frankly outlined some of the benefits to the oil industry, so frankly that Mr. Harvie at one stage asked him to repeat what he said.

Now the City, I say, has no assurance as far as Turner Valley is concerned as to the future, as to either supply or price and none can be given. Whether or not gas will be available from Turner Valley at least to the householders of Calgary depends on many factors and I suggest the principle one is not either capacity or willingness of the householder to pay for it. Take one instance alone that I refer to, the fact that today in spite of the best efforts of this Board and the best efforts of this Government as the necessary result of the oil industry gas is today being flared as I understand it at approximately 20 million feet a day and a little while ago it was 25 million feet. We know why.

THE CHAIRMAN: Still, that is a tremendous reduction, Mr. Fenerty, of waste compared with two years ago.

MR. FENERTY: Yes, but you see . . . . .

THE CHAIRMAN: We have done something, have we not?

MR. FENERTY: If this was a primary industry and the

oil was the by-product you would not have a waste of gas. You do not have any waste gas in a gas field. You produce it as you want it. But I will enlarge on that in a moment. All I am after at the moment is we have a primary industry and the flaring of gas after performing the necessary functions necessarily incident to it.

THE CHAIRMAN: Let us suppose that someone started a Fischer-Tropsch plant in Turner Valley and bought all the gas, we will say, at 10 cents a thousand, would the City of Calgary sit tamely by and see that happen?

MR. FENERTY: Would the City of Calgary then. . . . .

THE CHAIRMAN: Yes.

MR. FENERTY: I anticipate that by that time that the City of Calgary might be delighted to be relieved of that obligation and might be able to get gas at 10 cents a thousand in view of the developments that have occurred.

THE CHAIRMAN: But suppose it happened next year or next week, what would Calgary do?

MR. FENERTY: Mr. Stevens-Guille tells us what would happen. He says what we get is what is left from the absorption process.

THE CHAIRMAN: But supposing there is nothing left?

MR. FENERTY: Then we have to look around and see what we can get. It might be other counsel would register an objection.

THE CHAIRMAN: I think the City of Calgary would be setting up the theory that Turner Valley gas was dedicated to the use of the City of Calgary.

MR. FENERTY: The City of Calgary is not saying to you today that this Turner Valley gas is allocated to us and we

are going to have it no matter what we pay for it.

THE CHAIRMAN: You are not saying that to me today but I am suggesting under the circumstances I have mentioned, that you would be saying that.

MR. FENERTY: I do submit I am going to have enough trouble arguing this case on the facts of today without anticipating what will happen tomorrow.

THE CHAIRMAN: I have to take a broader view than that.

MR. FENERTY: Yes. What I am concerned with at the moment is our present position and I propose - I was going to refer to that very thing that you suggest, as to what happens when these other things happen. Now I ask that question: Why is gas being flared? Now I think I have the answer to it. That gas is being flared today because it is being produced under the Brown plan. It is being produced under the Brown Plan when there is no market for that gas because of the incidence of the place where the well is located. Today we have available for consumption just what is left after an absorption operation, without regard to quantity or quality.

Now in my brief on the next page I was going to deal with the very thing that you ask, and I will read this. "Who can say what will be the most efficient absorption gasoline operation in the future and what residue will be left? Already we have an application before this Board based on the premises that laboratory processes put into operation on a commercial scale would result in the use of all gas in something akin to the Fisher-Tropsch process, or an elaboration of it." Now that happened to be over the

page.

Now what is going to happen? Today we have a process - I do not want to get ahead of my argument, but we have a process in operation which so far as the heating efficiency of that gas, that residue dry gas is concerned, is harmful and I am referring to our present absorption operation. It is common ground as a result of that operation it results in a by-product with less B.T.U.'s in it and with less heating efficiency for heating purposes. The evidence is it is not as effective as if they left it alone.

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The City of Calgary is not complaining about that.

Now I am going to make some observations of the aggravation of the peak load as a result of that, but we are not complaining of it.

Now I say what happens, if the process in the future involves 50% in volume,- suppose it involves 80%, I do not know whether that is practical or not, but supposing it involved a larger percentage of loss in B.T.U.s and that is just what Mr. Stevens Guille says we will have, "We get what is left", and he refers to that at page 1264 in Volume 15. He did not refer to what would happen if it was 80% but he referred to what is happening today.

In other words, you have the manufacturing process and we get what is left, no matter how deficient it is in both quantity and quality, and there is no suggestion that there will be any rectification of that situation. If the B.T.U.s go down, it is just too bad for us. I know, in practice, we have certain benefits because it is a residue product but those are some of the disadvantages we have.

Now I want in that connection to talk about the absorption plant for a while. There was a suggestion at one stage, I think it has long since been abandoned, and I think it had to be abandoned in view of the evidence that the absorption plant was,as far as the dry gas operation is concerned, practically in the same position as the scrubbing operation, that is a necessary operation for supplying gas for fuel.

Now I do not intend to refer to the scrubber at all. We are all agreed that that is essentially a dry gas operation, and it is our full responsibility and the

full charges are proper chargos.

Now we have the evidence of several witnesses, and I suggest that theory was completely exploded, and that what we have now, if that absorption plant is not necessary to produce the kind of gas we require, then it necessarily follows it is a detriment to the dry gas industry because it consumes not less than 15% in quantity now and perhaps may go to 50% in quantity, and it also uses some of the essential B.T.U.s.

Now what is the result of that?

I think the same thing applies to the gathering lines. The fact is that the absorption industry has aggravated the peak load situation, a situation that the absorption industry complains of. We have the peak load requirement for the City of Calgary because we have 50 below zero in the winter time or something close to that at times, and higher temperatures in the summer, and there has been talk of that aggravating the situation.

But the absorption plant has aggravated it. It has aggravated it to the extent that the peak load must be 15% at least more than otherwise would be required because they take that much out of the gas that is delivered and some unknown percentage to me because of the reduction in heatiing units. For all I know it may be 20% or 25% of the whole. The peak load is directly attributablle to the operation of the absorption plant, and similarly it must necessarily follow that the 20 or 25 or 15% or upwards, whatever it may be, of the capacity of the gathering lines, is directly attributable to that also.

In other words, if you did not have the absorption industry you would have less peak load. You

would have less MCF burned because of higher B.T.Us. and you would have no excess gathering line capacity. Now that situation was very directly recognized by the B.A. Oil in its submission and I think it was recognized to some extent by Mr. McDonald.

I say to you, sir, that while we have the aggravated peak load situation because of the requirements of the City of Calgary, we have a further aggravation of that by reason of the presence of the absorption industry because the City of Calgary does not get the dry gas in its proper form. They take some of the B.T.U.s out of it and it necessarily follows that the size of the absorption plant is dictated by a perfectly proper, a proper commercial industry, to be able to treat every MCF of gas that is going to it. That is the situation.

Now that operation has in turn, although not to so very great a degree, affected the life of the field. If the gasoline industry uses up that extra amount, then it necessarily shortens the life of the field so far as the dry gas operation is concerned, and it has shortened the life of the field as far as the gasoline operation is concerned, just as much as the flaring of gas has shortened the life of the field as a gas operation, and both of those situations, I submit, should be reflected in the allocation of charges, and yet it now appears that the gasoline industry, which requires over the peak load, in excess of 15% above the City's peak load requirements, is now suggesting to this Board that that industry shall be charged only the same percentage of costs of gathering as is represented by its own additional peak load requirements without any consideration of the facts pointed out by my friend, Mr. Steer,

that it uses the whole 100% in any event. Its 15% on the volumetric basis is just about the same as the 15% of the peak load requirements.

I perhaps should deal with that a little later somewhat further in connection with the division of the operating costs, but I just want to finish up my argument first as to the City's position.

I want to point out that this dry gas which we are interested in is not a product manufactured to a suitable specification. It is a residue or waste product that may or may not be of value in the future either, because of deficiencies in quantity or quality. In other words, it is what we have left after you manufacture some commercial product to definite specifications.

Now the next thing I have to submit to the Board is that Turner Valley gas, - I am speaking now of dry gas, - is and always has been a by-product or waste product arising from oil or gasoline operations.

It is suggested that because of existing legislation, Turner Valley dry gas is no longer a waste product. I suggest to this Board that if there is other gas available, it is completely valueless to the consumer if it costs more than the other gas, and as far as repressured gas is concerned, it is only of value to this some unknown consumer at some time in the future, not less than 15 years hence, and then it is of value to that unknown consumer only if there is no other gas supply available to him at a lesser cost.

It is valueless, I suggest, at all times when there is excess production, and it is less valuable than ordinary gas produced for fuel purposes at all times because it is produced as an incident of an oil operation at a location

which has no economic relationship to the fuel gas operation and is produced without regard to market for the gas or absence of market, either because of location, which necessitates flaring or because of the time of production when there is a surplus.

Now, I am refering to its value at the place of production and not its value at the scrubber. I propose to advance an argument to you presently that all of this gas has one value at one place and that is at the entrance to the scrubber.

Now I say to you, Sir, that it is necessarily a by-product under the Brown Plan. I suggest that the Government of the Province of Alberta in giving effect to the Brown Plan, or the Board, the Conservation Board, in giving effect to the Brown Plan has said that this gas has performed its economic function just as in Texas, you know, the gas lift involving ten thousand feet of gas per barrel, is deemed to have performed it economic function.

Now if that gas has performed its economic function under the Brown Plan, and I submit that is the justification for the Brown Plan, it necessarily follows that it is a by-product and that, by the way, was Dr. Katz' view. He treated it as a by-product if it had performed a certain function in the gas industry.

Now here is a way of doing it the other way, we can take the Brown Plan as one of two things:

It is either a scientific plan for the production of oil, and which is not designed to produce gas, dry gas, or even wet gas, in the quantities required and as it can be used, or it is an unscientific plan to waste gas. It has to be one or the other. It is a plan which produces gas

at a time when there is no market for it.

Now if that is so, it is either a scientific plan to produce oil or an unscientific plan to waste gas, and I prefer to suggest it is a scientific plan to produce oil.

Now if the Brown Plan is a scientific plan to produce oil, involving a by-product, then that by-product cannot be anything else but a by-product when regulation of the same operation is being further considered by the Government.

You just have to look at this Brown Plan and the operation of it with the same glasses.

Here again it is a by-product for a number of reasons:

It is recognized as a by-product by all parties when they agree that a cost approach with rate basis for wells and different costs is completely unsound.

In a gas field where wells are drilled for gas production, that is recognized as the proper approach. The cost of those wells must necessarily be considered and amortized if the industry is to continue to exist. I say again it is a by-product for another reason, because it is not manufactured to a specification but is what you have left following the manufacture of the principle product to a specification.

It is a by-product because it is being flared in places where it is a choice between oil operations and gas operations.

There is no flaring of gas, we have that evidence repeatedly, in a dry gas field as such. The cheapest place to store it is in the ground, to store it there

and use it as you want it, and just as soon as you flare this gas when there is no market for it, it becomes a by-product. It cannot be anything else.

And it is a by-product of an oil operation. It is that throughout, as long as, I say, you got what is left without reference to quality or quantity. It is common ground that Turner Valley was developed as an oil field and it is still being developed as an oilfield .

(Go to page 7210).

I suggest to you that as the result of gas dissipation as an incident of oil operation that field can never be economically further developed as a gas field, if indeed it ever could have been developed in the first instance as an gas field. The problems are wholly those of an oil field. As I pointed out you do not have repressuring in a gas field and I think everyone agrees that waste gas is an incident of an oil field operation. Certainly Dr. Katz, at Pages 612, Vol.9 and Stevens-Guille at Pages 1264, Vol.15, feel the same way.

Now we have evidence that in other jurisdictions that approach is well recognized, so far as repressuring is concerned. Mr. Ralph Davis points out at Pages 331-335 that the invariable practice is that the producer undertakes repressuring as an incident of his oil operation. And I say that Mr. Zinder recognizes that repressuring is entirely an incident of oil operation. At Pages 4002-14 and 4019 in Volume 51, and I say not only is repressuring recognized as an obligation of the producer but it is claimed as a benefit by the producer before this enquiry as a benefit. It is recognized as an obligation and it is claimed as a benefit. Both the G.O.P. and the B. A. Companies ask that gas in excess of market demands should be returned to the same part of the field from which it is taken. Mr. Mahaffy referred to it as a matter of vital importance. That was at Page 484, Volume 6.

Mr. McCutchin of the B. A. Company attached great importance to it. At Page 26 he outlined nine benefits attached to the operation in the south end of the field to the industry. My interpretation of that is that all but one are solely benefits of the oil industry and that one also benefits them. Ralph Davis says at Page 851 in Volume 11 that it is

primarily an oil and wet gas field. Mr. Mercer on cross-examination at Pages 2766 and again at Page 5777 agrees that Turner Valley is an oil field first, last and all the time.

At Page 35 Mr. McCutchin outlines the benefits of repressuring to the oil operators as well the benefits of the new installations to oil operators.

Frank Reeves, whose evidence was referred to here this morning says, and this is the way he puts it, that the oil operators have waited for years to get a low pressure line. That I say was the voice of the industry and not the voice of the City of Calgary. The City has not waited for a low pressure line for years.

THE CHAIRMAN: But the City of Calgary did ask the Gas Company to augment its supply some years ago and they will do it again if it is called upon.

MR. FENERTY: Let me say that when the question of augmenting a supply comes up we may have many arguments as to why the City of Calgary should bear some share of augmenting the supply, but I say augmenting the supply has nothing to do with the prevention of the dissipation of the supply already available. I am going to come to that.

THE CHAIRMAN: It is your attitude of cold aloofness to the whole proposition.

MR. FENERTY: Yes, but it is very significant that the only principle that any of my friends can find in poring through the text books to justify the consumer of today bearing some expense in connection with repressuring and so on is the development of new sources of supply. And yet what is being done here is not dissipating the old sources already developed. It is the converse of what they are talking about but still that is a trifle, I am coming to that later.

Now I want to emphasize again my learned friend, Mr. McDonald, outlined three principal benefits and said with the utmost frankness as to the substantial benefits to the oil industry. He outlined that two or three principal objects of the Act were to provide a market for all producers and to provide an access to that market for the producers. Those are both oil operators' benefits. Just nothing else, plain and simple. He did not surely advocate providing a market for the producer at the expense of the consumer. Is there any reason why the consumer should pay more for gas in order that someone else should get a market. I cannot follow the economics.

Here is the picture of Turner Valley, I say set out in the evidence of Mr. Stevens-Guille on cross-examination supplemented by some other evidence because there is one of these propositions Mr. Stevens-Guille did not have the information about and he did not give me the answer to it. But his evidence in the main supplemented by the evidence of one or two other witnesses is this, that no well was drilled in Turner Valley into the limestone for the purpose of getting gas. You will note that I am not taking in too much territory. I am talking about Turner Valley only.

MR. STEER: That is unkind.

MR. FENERTY: I may be open to something myself yet.

And that every well drilled into the limestone was drilled for the primary purpose of getting oil. So far as is known no well in Turner Valley has ever been abandoned because it had to flare its residue gas, or, in other words, it had no market for its residue gas. Again, no well in Turner Valley has ever continued in operation without obtaining some

returns from either crude oil or gasoline, and wells have been absndoned in Turner Valley where it was still possible to get gas from them.

Let me put that picture together. I am not going to suggest what kind of operation it is.

Mr. Stevens-Guille is found at Pages 3381 and 3382 in Volume 44. There is one thing he did not contradict, but he did not have the evidence, but that is amongst other evidence.

I now want to refer a moment to the Home Company. I trust I made my suggestion clear in the elaboration of those wells drilled and the object of the operation.

I want to refer a moment now to the Home contract. I suggest that the cross-examination of Mr. Kirkpatrick and his answers at Page 2171 make it abundantly clear that that was a contract entered into from a wet gas point of view.

It is true that it may conserve some gas cap gas at times of peak load. On the other hand it creates a headache in warm weather as involving some extra repressuring and why is there some repressuring ? Because the absorption plant does not treat the Home Gas or otherwise it would not be down here.

MR. CHAMBERS: I think it is fair to say, and I think the Board will agree that if that contract had not been entered into there would have been an order of some kind from the Board.

MR. FENERTY: That may be information I do not possess. I am speaking now from the record.

MR. CHAMBERS: I think that is already in the record.

MR. FENERTY: Well the fact remains that it is common ground that so far as the Home Gas is required that gas as such will not be required for some fifteen years and at the time it is required, if it is required, then it may not be available and the present benefits are to the absorption gasoline industry with some conservation in the gas cap at peak load and some repressuring in times of minimum load.

Now my friend, Mr. Steer, referred at some length to the change in the situation when the gas became so rich that the absorption operation apparently was a beneficial operation from an absorption point of view and he referred to the amount of gas flared in excess of market requirements for dry gas as a result of an oil operation and flared at the absorption plant as a result of a gasoline operation. Mr. Stevens-Guille at Page 3349, in Volume 43 did mention as I have it that in the years 1933 and 1934 in the north end gas was going to the absorption plant in excess of the Canadian Western requirements.

Now it was being gathered in excess of the Canadian Western requirements when he says in excess of Canadian Western requirements and it was being flared. I take it it was in excess of 15% of Canadian Western requirements. That is what was going through as a result of the absorption operation.

Now a couple more points on this question of what kind of an operation this is.

Mr. Stanley Davies in his evidence indicated that the value of oil and gas produced up to the present time exceeded the value of gas as computed on the prices obtained in the ratio of more than ten to one.

I want to elaborate just a little on what

Mr. Steer said that Mr. Stevens-Guille said with reference to the Royalite operation.

I suggest his admission, not his statement, in answer to a question found at Page 3341 in Volume 43, and I suggest that puts the situation exactly. That the Royalite was conducting an oil and gasoline operation and was fortunate in having a market for its residue gas; whereas the B. A. and G. O. P. Companies were conducting the same kind of operation and were unfortunate in not having a market for their residue gas.

That I say is a perfect comparison. One is fortunate in having a market for its residue gas and the other is unfortunate in not having a market, and it cannot change the nature of the operation and I cannot improve on that larguage.

Now some witness, and I have not the reference here, but I do not think there is any dispute about it, pointed out that the wells in the north end that could not get on the gas line at 300 pounds pressure in winter held the separators at 300 pounds and flared their gas.

Now I think I am correct in that witness' statement, Unfortunately I have mislaid that reference.

What kind of operation is that? They had a choice between not using the well, not wasting, just not producing it, or wasting the gas. It was not a case of wasting oil. It was a case of not producing oil at that particular time or wasting gas. And what did they do, waste gas. Can anybody call that anything but an oil operation.

I repeat that the operation of this field so far as production is concerned has been dictated, leaving

out the Board's direction, leaving out directions or orders given by this Board and the Government, so far as the operators are concerned has been dictated solely by oil and gasoline requirements.

There is no purpose in elaborating that any further. I say it follows from what has been said that dry gas is necessarily a residue product and where overproduced until recaptured and stored it is necessarily a waste product.

(Go to Page 7217)

I therefore submit that residue gas in Turner Valley cannot lose its characteristics of gas by legislation, and I submit that it will continue to be a by-product unless and until the present situation is reversed, and oil and gasoline are produced and manufactured only to the extent that production is available after first providing for gas requirements day by day, both in quantity and quality. If you get that state, I will admit it is a primary product. There is your test of primary products and by-products, what you manufacture and what you have manufactured for that market, and just as long as you are manufacturing oil and gasoline for the specifications of the market, and not purely dry gas, whether there is a loss in the B.T.U., and no matter what the Legislature itself says, it is a by-product. And I say that it is a by-product under the Brown Plan, because the Brown Plan is a plan to waste gas because it provides for the flaring of gas. And I say that is not the situation today under the Brown Plan under which this gas is produced, and if dry gas is a residue product or waste product under the Brown Plan to which this Government is committed, as I said before, it is the same kind of a product when we are considering it in relation to further regulations.

All matters of Government policy relating to the same subject matter must be looked at through the same glass. Legislation cannot change the nature of the operations, and it cannot change the location of the wells, It cannot change what dictated their location.

And I want to emphasize again that until such time as the gas is treated as a primary product, and manufactured as a primary product, it is going to be necessarily and must be a by-product.

Now, I want to come for a moment to what seems to me to be a schoolroom subject, and yet it has been dealt with before this Board. The subject which I submit is a school room subject, because it certainly has no practical application amongst practical men in the considering of our problems, is this thing called the intrinsic worth of gas. And there may be some error in my reasoning, but I cannot help feeling that my friends appreciate where this theory of intrinsic worth of gas leaves them or they would not have introduced it. I might be wrong in my reasoning. My reasoning might be fallacious, but that is the way it seems to me.

I say this theory of intrinsic worth of gas is an attempt to escape from the results inevitably flowing from the fact that Turner Valley dry gas is wholly a by-product of another industry. And in order to escape from the results flowing from that fact that Turner Valley dry gas is wholly a by-product of another industry, witnesses such as Mr. Zinder were called to evolve the theory that gas as such has an intrinsic worth, and that is, as I understand their theory, that the gas as such has an intrinsic worth, irrespective of its location, marketability, or cost of handling.

I suggest that this is a vague and nebulous idea suitable for discussion in classrooms but is wholly incapable of application in practice and certainly incapable of application in a field where we see burning today 25 million cubic feet per day unavoidably as an incident of oil operation. What is the intrinsic worth of that 25 million cubic feet per day of gas that is being flared today? Should the intrinsic worth be charged as an operating loss to those well owners? It is just plain common sense, I submit.

Let us take something that is not in evidence as an illustration, but in any mind, well, not maybe in any mind, but many minds would consider it as an apt illustration. Let us take the immensely valuable and famous Sullivan mine at Kimberly. I think it is common knowledge that they have a complex ore there, containing several valuable minerals, and that until the late Dr. Blaylock evolved commercial processes or systems of treatment that cost less than the market values of the resulting minerals, they were worthless and incapable of development. It had to be developed to bring out the values in that ore, comparable to the values of those minerals elsewhere, otherwise economically that ore was worthless. And until that time the Kimberly mine was not developed.

Now, as I understand Mr.Zinder, he says, and he must say, that that ore, and in this case, the gas, had an intrinsic value, and they must be worth something more than the value established by the ordinary law of economics and trade and commerce.

Now, if there is one place where gas has an intrinsic value, it is in the dry gas field. And there is a place where it has a primary product, where it is a primary product and not a secondary product, and we have got that place right in Alberta, the field adjacent to Edmonton. There is a place there where you have the dry gas and there it has an intrinsic value. It is not a waste product. It is not a by-product. It has got an intrinsic value as gas there.

Now, if that is so, are the prices for a primary product, and it is a primary product in the Edmonton field, can those prices at any time be less than the price of a by-product, if on the theory of intrinsic value they should

be the same? I would like my friends to think about that. Is the Board justified in fixing a rate higher, a higher rate, than the intrinsic value of gas, and I am referring now to the Edmonton value, a higher rate in Calgary than the intrinsic value of gas merely because there are additional problems here and resulting costs arising directly from the fact that we have here an oil field and an oil operation with resulting costs not found in the Edmonton gas field. You see, what my friends are going to work out here. We are going to have a higher price for a by-product of an oil field than you have for the primary product of the gas field. So much for the intrinsic value.

I say that such a suggestion is not only a complete negation of the intrinsic value theory, but it necessarily results in the City of Calgary being committed indefinitely to the support of the Turner Valley industry. In other words, we are going to pay for this being a by-product. That is the reverse of all the economical laws that I have ever heard of.

Now, I want to refer for a few moments to the general principles that are involved, I submit, or should be applied to oil well operations with dry gas as a by-product. Now, I am going to make a suggestion here about starting where you find dry gas, and I am going to speak at some length with regard to it, and I want to say at the outset that I realize there are certain difficulties in it. Those difficiulties, as I see them, and are the only difficulties as I see them, are in the fact that certain installations upstrram from the place where you find dry gas, in the North End, have been ordered, and certain installations in the South End have been orered. I prefer to say in that case they have been permitted,

but in the other case there has been an Order of the Board, and we must recognize that there must be some protection given in connection with those installations that have not been installed by the direct initiative of the oil industry or the gasoline industry. But I say that this argument is a factor in considering the allocation of costs with reference to those installations, and I say it is a proper argument in excluding the costs of the other installations. But I am quite prepared to admit, in frankness and in fairness, that the new installations sanctioned by the Board must be given consideration outside of the scope of this argument.

Now, with that explanation I suggest to this Board that on the basis of dry gas as a by-product of the oil and gasoline industry, assuming that is established, and assuming that the Board agrees with that, I suggest that a starting point must be at the place where that article of commerce is found, and that the price that is being presently paid for it, and as we go along we will see where we go from there, and this Board was concerned somewhat about the starting place, we are going to start at the bottom of the well and work up.And I will elaborate on that. But I am starting on the well known economic theory that when you have something established you must find a very sound reason for changing it, and I thinkall economists agree with that.

Now, that starting point where it is found here is that the Canadian Western mains, no, pardon me, it is not the Canadian Wextern mains, it is at the exit of the scrubber, $7\frac{3}{4}$ cents, which is the intake of the Canadian Western main, or it is at the exit of the absorption plant where you have that $7\frac{3}{4}$ cents less the scrubbing costs. They come to the same thing in the end.

Now, I say further, not only is that logical and sound that you start where you find the creature but that is what the Act says, and I am just going to refer to it for a moment, and I refer to Section 72. I might say now, that I do not propose to cite any English authorities of what can be done or cannot be done or anything else. I propose to talk about the Act of 1944 as amended in 1945. And that is our yardstick as far as this Inquiry is concerned. We will stick to that.

Now, Section 72, and we have here subsections (a), (b), (c) and (d), says;

> "Notwithstanding the terms of any contract, the Board may fix and determine"

and you will remember it was amended. It did read "shall" and it now reads "may". It reads:

> "Notwithstanding the terms of any contract, the Board may fix and determine a just and reasonable price or prices for natural gas in its natural state as and when produced from the earth at the gas exit from the separator,"

and in all other cases at the well head. Well, that is not the thing we are talking about today, gas in its natural state at the exit of the separator or at the well head. That is a matter of inquiry, obviously, between the well owner and the absorption industry, that 80-20 per cent. We are talking about dry gas and everybody is apparently obsessed with the idea that we look for dry gas at the well head, and we start considering the dry gas at the well head, and there is not just any such animal.

And here are the other two, a "just and

reasonable price or prices to be paid for natural gas, which has been gathered and delivered to an absorption plant and after it has been subjected to treating or processing by absorption, or otherwise, for the extraction, therefrom of natural gasoline or other hydrocarbons."

Now, that is the proper subject of inquiry here, the just and reasonable price of the gas that has already been gathered.

And then there is subsection (c),

"A just and reasonable price or prices to be paid for natural gas after it has been scrubbed or otherwise for the extraction or removal therefrom of sulphurotted hydrogen."

Now, I say the scope of this inquiry with reference to the dry gas is the price at the exit of the absorption plant, plus the scrubbing price. That is what the Act says. If it had intended anything else it would have said so.

And then the other section deals with the subject that we are not going to pay for wet gas, at least, I hope we are not going to pay for it, and won't be paying for it.

MR. McDONALD: Have you given consideration, Mr. Fenerty, with regard to the addition to Paragraph (a) that has been added by the amendment of 1945?

MR. FENERTY: Paragraph (a). Just a moment. I think I did.

M . McDONALD: The section here under the amendment?

MR. FENERTY: You mean where it says "By striking out the words"?"

M. CHAMBERS: No, not that.

MR. McDONALD: The next section (b).

MR FENERTY: Not including the component parts of the gasoline?

MR. McDONALD: Yes.

MR. FENERTY: You do not include the component parts of the gasoline because you start with the exit at the plant. That is just my argument.

(Go to page 7225)

How can you start somewhere else? You must take the gasoline out and I included it. I have to thank my friend for that. I had frankly forgotten that. You do not include the absorption gasoline price because to start with the Act says that the absorption gasoline is out of it. It is dry gas we are talking about and that is the price we are interested in. I realize in an Inquiry between a well-owner and the absorption industry the just and reasonable price of that wet gas is your 80-20, but we are not in it. We are not in it unless we get part of the gasoline content and I do not think anybody wants to give it to us.

MR. CHAMBERS: Pardon me, I would like to get this clear because I may have something to say about it. Do I understand under 72-1(A) you say the Board has not to fix the well-head price?

MR. FENERTY: The well-head price of dry gas?

MR. CHAMBERS: Yes.

MR. FENERTY: I do, certainly. Because there is no such thing. If anybody can find any dry gas at the well-head in Turner Valley, we will probably get an amendment to the Act. At the moment we talk about dry gas at the exit of the absorption plant. We talk about it there because there is no other place you can get it in Turner Valley. I think I am right in saying there never has been any dry gas although we all know in this gas industry when the gas was too lean to put through the separator, they still put it through the absorption plant and got a greater gasoline content because it had not gone through any separation process in the first instance. Some of my friends around me know what I am talking about.

But even if the Act did not provide for starting where you find dry gas, when you are talking about dry gas, and if you contemplated something more than finding dry gas at some place where you do not find it, what reason and what basis do you use for starting anywhere else? There is no stopping point short of the bottom of the well. Why would you start at the exit of the separator? This gas did not start there. If you are going to throw overboard the place where the dry gas starts, where are you going to start? I know of no place except the bottom of the well and we are all in agreement we are not going there. I submit that and I say again, all these arguments are subject to this that some allocation and adjustment must be made and properly made with reference to the installations ordered and they must be paid for on such a basis as the Board finds reasonable because they were ordered as an incidence of the dry gas industry. I say that argument is logical and sound and in accordance with the Act, at least insofar as everything that was installed by specific order and direction of the Board. I say that insofar as the low pressure gas system is concerned, while I was not in the Inquiry when that order was made, my reading of the evidence is that the British American Company was seeking a privilege on the basis of assuming a risk and was not carrying out a mandatory order of this Board. If the British American was seeking a privilege and I can understand why they would be, with a three year life as compared with perhaps a 15 year life, I suggest that that part of the installations should be subject to the rule of old installations and that to that extent I say that this must be treated as something which we find at the downstream side of the absorption plant.

That does not affect scrubbing or re-pressuring. First, scrubbing. We admit freely and frankly that is entirely incident to the dry gas operation and must be paid for in full. Repressuring, I suggest, is solely incident to the oil operation and is still incident to the oil operation, even though this Board may not be prepared to give effect to my argument insofar as gathering lines are concerned. In other words, I say that repressuring is in entirely a different category from gathering.

I suggest to this Board that the G.O.P. submission or the G.O.R., I am not sure which it was at the moment, that submission is the only logical one that can be made with reference to every installation other than those constructed under order and what I think in effect they are saying is that what has taken place is an oil and gasoline operation with a free handout of whatever returns there may be from the waste product, which was not in contemplation by them.

That is, in turn, subject to some qualifications because I cannot shut my eyes to the evidence, the uncontradicted evidence here, that as to the North End of the field and as far as the Madison Company is concerned the evidence seems clear that some of these operations were not dictated solely by the requirements of the gasoline industry and they have pointed out that with a normal absorption industry, this plant would have been of smaller size and would not have involved a 24-hour operation and so on, and they must be given some consideration insofar as that part of their installations might have been affected by the necessities of the City of Calgary. I do not know

just how you work that out but I agree there is that difference between the North End and the South End. I said a moment ago the impression left by one reading the evidence was that the British American Company was seeking a privilege with any attendant risk there might be, which it was willing to assume and was prepared to take, and apparently never regarded the installation of the low pressure lines as imposing a burden on them or on the consumer. I refer in that connection and I am going to skip over it, the G.O.P. I say is in the same boat and comes to this Board and says so. Mr. Carr, at pages 265 and 266 in Volume 5, Mr. McCutchin at pages 221-226 in Volume 4.

This matter of assuming the risk, page 420, Volume 6.

The matter of no increase in price to the consumer, see pages 417 and 418 in Volume 6 and for other references, may I refer to pages 154 to 159 in Volume 3 and 162 and 163 in Volume 3 and page 234 in Volume 4.

Now Mr. Denton pointed out, I think he did, that is the way I read it, that the gasoline contents were higher in low pressure gas, indicating additional benefits to the gasoline industry on the installation of low pressure lines. His evidence is found at page 384, Volume 5.

As I mentioned before, Mr. Reeves said that the oil industry had been waiting for a low pressure system for years. Pages 149 to 151 in Volume 3.

I just invite consideration of this situation which was disclosed during the evidence with reference to supplying fuel. I thought it was significant. That is in supplying fuel in the field for drilling purposes.

You may remember some cross-examination of a witness on that point. Here is a well with gas and a well across the fence, as we put it, drilling. That gas is piped as much as 11 miles to the absorption plant and 11 miles back to the well across the fence. I asked why did they not just tear out a couple of pickets and put the pipe across the fence and the answer was in effect because it would be an economic proposition the other way. What was happening was, there was an economic proposition to pipe that gas 11 miles to get 80% of the gasoline content and it was an economic proposition to pipe it 11 miles back to get 20% of the gasoline content because when they got there they sell fuel for exactly the same price as before. That was economic from the point of view of the well owner and the gasoline industry. 22 miles for 100%; 11 miles with 20% and 11 miles with 80%. Is it any wonder if it pays a well-owner to pipe it 11 miles to get 20% that the gasoline industry is willing to ask nothing better than the privilege of paying all the carrying charges in order to get 80%. If the well-owner could do it for 20%.

That brings us to the point of the consideration of the fact that transportation to the absorption plant has been paid for out of the present 80% of the gasoline content going to the absorption plant. The owner is entitled to 20% at present and entitled to such proportion as may be fixed by the Board, if it is more or less and it will vary. In any event, the owner is not concerned with transportation because he is not interested in it, because he sells f.o.b. the well.

Now as I interpret the absorption industry's contention today, it now proposes, because of the passing of

some Act and this Hearing to retain the 80% of the gasoline content that more all the carrying charges and pass on 85% of those carrying charges to the consumers in the City of Calgary while retaining the 80% benefit. My recollection is that Mr. Donellan and I think Dr. Stewart and Dr. Katz agreed that if the carrying charges were going to be borne by the consumers, they were entitled to a share in the gasoline content.

Mr. Donellan's evidence in particular, I think, is to the effect that the 80-20 division was considered fair at all times and that whoever bears a share of the gathering costs is entitled to share in the gasoline content. I refer to the evidence at page 3191 and 3194. That is not the operators' proposition nor is it the gasoline industry's proposition. It is not proposed, as I understand it, to have the consumers share in the gasoline content which were described by counsel before this Board as vital to the refinery operations and I suggest to the Board if the consumer is to be excluded from the benefits of the gasoline operation, he should be excluded from the obligation already assumed by that industry with reference to both and that is the transportation charges and the 80%. There can be no economic justification of any industry given 80% on the basis of bearing all the carrying charges and then on the basis of fairness and justice asking this board to pass 85% of those charges on to the consumer of dry gas while retaining 100% of the gasoline content. That is the proposition that is being put to this Board and apparently seriously being put to the Board.

MR. HARVIE: Not by our Company. That was not the

proposition put by our Company.

MR. FENERTY: I agree with that. At the moment I had forgotten. Now I say again excepting new installations the proposition that that should be borne by those who are retaining the benefits or an adjustment of the oil industry, in that case by the oil industry partially, it imposes no hardship. We know now we have not got the exact evidence - some of it was shut out and the other was not available - but we know now that with the exception of new construction the gathering lines has been paid for and substantially paid for. We suspect 60 to 70% paid for and paid for out of the expense of the gas reserve and the shorter life of the field and therefore necessarily higher operating costs. You see these very installations used in connection with this particular field have been paid for as a result of this gas being used and the by-product flared. It is just as much a by-product as the carbon that goes out in the flame of your furnace and because it was used, 100% of it was used and the by product flared and I say they have paid for their installations and at the expense of the gas dealer.

(Go to Page 7232)

because they have blown off that gas I am not complaining of it but that is the result of it and now Dr. Stewart says that results in a higher operating cost. They have in effect paid for their installations at an increased cost to the consumer. No way out of it.

Now Dr. Stewart says at Page 4449:

"Where operations have been conducted at the expense of the gas field'

and that is exactly this:

'the gas field is entitled to some compensation."

Mr. Ralph Davies is thinking along the same lines, although in relation to and discussing conservation rather than gathering, when he says, at Pages 346 and 347 of Volume 5, that conservation should not be at the expense of the consumer, because of the way that the field has been man-handled;

and I cannot help thinking that any result that is arrived at by the elimination of the past, and a consideration or a refusal to consider what has been done to this field at the expense of the dry gas industry and to the profit to be gained to the wet gas industry and the oil industry, resulting in the payment, almost payment in full for their equipment, which we are now considering, - I say that any failure to consider those factors must result in inequities and unfair results to the dry gas industry.

As my friend, Mr. Steer, put it perhaps much more aptly than I can, it has been an integrated operation and you cannot separate them merely for the benefit of those conducting the integrated operation to the prejudice of those who are at one end. It just cannot be done in reason and

fairness and justice and after all that is what we are here trying to do.

Now my suggestion that you look at the exit of the absorption plant, where you find the dry gas, perhaps might be taken as implying some criticism of the taking over of the gathering line by the Madison Company. I did not hesitate to make some criticism of that proposition at the beginning. I thought it was unfortunate. I was probably quite in error, but I could see no reason for it from the explanations given and to me it seemed obvious that the result of doing it was most unfortunate in that the extent of the line which had already been paid for, - I have nothing to say of the lines of the new construction because they have not been paid for, - but to the extent of the lines which had already in part been paid for, the result would be to shoulder and impose a burden upon the shoulders of the consumer, resulting in him paying for them again, a burden which should not be his.

Now I want to just say a word about the explanations given by Mr. Stevens-Guille for taking over those lines. We had a lot of passages about it and in this connection I am going to point out that the fact that the Utility has a line does not require this Board, - we did have a provision in this Act which says that the Board "should" determine prices and so on and we changed it to "may",- and that will prosently appear in this argument about the divided rate base, but I say it is not absolutely necessary for the Board to take into consideration everything that the Utility chooses to acquire and it certainly is not necessary to consider the utility operations in connection with the absorption gasoline, which I

will come to presently.

Now I say that Mr. Stevens-Guille's evidence, and as I say we had a lot of differences about it, quite a lot, but I say his evidence boils down to just one thing, and I say again and I mean it, a single unconvincing reason for taking over the gathering line, and I say this, and my friends will show where I am wrong, if I am wrong, that his final explanation is, and after cross-examination, - it is found at Pages 1994 to 1996, of Volume 25, and his explanation I say actually is that the Madison Company has two or three employees who were former employees of Royalite who can correlate the operations.

I am not going to make any comment on it. I am just going to say that is what he said. My comments I submit would be superfluous.

Now I venture to suggest that my learned friends will quarrel with Dr. Stewart when he says that the gas field is entitled to some compensation for what has been done to it by the oil industry, if anything has been done to it, particularly where it resulted to the profit of the oil industry or the gasoline industry and if I understand the situation, and the contention, advanced by the industry here, it is that not only is the gas industry and the gas consumer not entitled to some consideration as the result of those operations and those profits made,- not only are they not entitled to participate in those profits in the future but they are going to have burdens added to them now as the result of the way it is proposed to conduct these oil and gasoline operations in the future, involving repressuring and other costs which are not an incident of the dry gas operation.

Now I want to go to the price of the gas

at the exit of the absorption plant.

THE CHAIRMAN: Mr. Fenerty, when you speak of "repressuring" can you tell me who paid for the repressuring in Bow Island ?

MR. FENERTY: I am dealing with that in a moment too but I will say right now what I had in mind.

I would say the repressuring in Bow Island is an entirely different proposition but on my friend, Mr. McDonald's theory as to storage, and as I say I am going to repeat it in sequence in my argument, - we are going to have them moving gas, wet gas, from one storage place to another in the same field. You can call it "conservation" but that so far as the Bow Island field is concerned itself, that repressuring definitely is not a result of moving gas from one part of the field to another. It is an increased supply and I agree that my arguments as to repressuring in Turner Valley do not apply to the Bow Island field but my arguments as to the way that repressured gas should be paid for, that is the way it is proposed to be done in Bow Island, certainly do apply to Turner Valley.

THE CHAIRMAN: Is there any guarantee that you are going to get all the gas out of Bow Island, that you put in ?

MR. FENERTY: No, but there is one justification for it and that is that it is creating a reserve in the Bow Island field which was not there before, but it is not doing that in Turner Valley.

MR. CHAMBERS: It was in Turner Valley before.

MR. FENERTY: What they are doing in Turner Valley is not what they are doing in Bow Island.

MR. STEER: And I am not sure that the evidence is that we will not get it. I am inclined to think that we will

get it in Bow Island because it is an excellent formation.

THE CHAIRMAN: There is evidence too as to the gas cap, the Royalite gas cap.

MR. DAVIES: It is the opposite way. In Bow Island it is an open formation and in Turner Valley it is a tight formation.

THE CHAIRMAN: Yes, but it is an open formation with limits.

MR. DAVIES: Yes, with water surrounding it.

THE CHAIRMAN: It is the same thing as a tight formation, the gas cannot escape.

MR. FENERTY: I will put it this way: there may be some justification for the consumer being charged with possibly repressuring operations in Bow Island, charged, as both the Royalite and the Gas Company contemplate, when he gets the gas, that is when he is going to be charged, that is what the Royalite said they were going to do,- as I say there may be some justification for that but there is nothing in reference to the storage when you are shifting gas from one place to another, so that the oil industry will benefit.

THE CHAIRMAN: I imagine though, Mr. Fenerty, that the Gas Company, when it buys gas from Bow Island, that cost goes through as a gas purchase.

MR. FENERTY: Yes.

THE CHAIRMAN: And when they use a compressor to put that in the Bow Island formation - -

MR. FENERTY: Yes.

THE CHAIRMAN: That goes through as an expense and that is reflected in the price which is paid for gas in Calgary, the consumer pays for it.

MR. DAVIES: Now it is capitalized. We pay a return on it but it is not paid for until he gets it.

THE CHAIRMAN: I know but the costs of doing all that are paid for. It is expressed in the rate. The costs of the purchase of the gas and the costs of repressuring.

MR. FENERTY: As distinguished from the price of it, that is true, but it is a minor argument, and what the costs are I do not know, that is I am not much concerned with that except to show that what is done in order to give you a greater supply in Bow Island cannot possibly be used in relation to the shifting of an existing supply from one part of Turner Valley to another so that the oil industry will benefit and that is what my friend Mr. McDonald says he is doing.

As there are only a couple of minutes left before adjournment, Mr. Chairman, I wonder if it is worth while for me to start another subject or for me to start on a new phase of this.

THE CHAIRMAN: I do not think you should start a new phase now, Mr. Fenerty.

We will adjourn now.

(The Hearing was here adjourned to be resumed at 10 A.M. Wednesday, June 19th)